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Supreme Court, U.S.
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No. _____

In The

Supreme Court of the United States

October Term, 1993

CONTINENTAL POTASH INC. and CROSS LABORATORIES, INC.,

Petitioners,

v.

FREEPORT-McMORAN, INC., FREEPORT MINERALS CO., and NATIONAL POTASH CO.,

Respondents.

Petition For A Writ Of Certiorari To The Supreme Court Of The State Of New Mexico

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Whether, under the Supremacy clause, a state may adopt as a matter of state law a rule that, as to an assignor of mining rights under the Mineral Leasing Act of 1920, 30 U.S.C. 181 *et seq.*, highgrading (the removal of the best ore first leaving remaining ore commercially unrecoverable) is beneficial and hence not actionable, even though such activity constitutes waste under applicable federal regulations incorporated into the contract of assignment.

2. Whether, under the Supremacy clause, a state court may ignore federal law in construing a private contract of assignment of mining leases under the Mineral Leasing Act where the contract expressly binds the assignee to comply with federal law and regulations and is made "subject to the requirements of the (federal) leases" which by law, 30 U.S.C. § 187, must contain provisions requiring the lessee-assignee to exercise "reasonable diligence, skill and care" and prevent "undue waste."

3. Whether, under the due process clauses of the Fifth and Fourteenth Amendments to the U.S. Constitution, a state appellate court may ignore trial court and jury findings that highgrading was wasteful and damaged assignors of mining rights under the Mineral Leasing Act of 1920, and otherwise substitute its own findings for those of the trier of fact, when such findings are based on substantial evidence.

PARTIES TO THE PROCEEDINGS

Petitioners are Continental Potash Co., Inc., and Cross Laboratories, Inc., both standalone companies without parents or subsidiaries.

Defendants are Freeport-McMoran, Inc., and its subsidiaries Freeport Minerals Co., and National Potash Company.

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Respondents.

Petition For A Writ Of Certiorari To The Supreme Court Of The State Of New Mexico

PETITION FOR A WRIT OF CERTIORARI

Petitioners pray that a writ of certiorari issue to review the Opinion of the Supreme Court of New Mexico of August 10, 1993.

OPINION BELOW

The Opinion of the Supreme Court of New Mexico appears at 858 P.2d 66 (N.M. 1993).

JURISDICTION

By unpublished Decision April 22, 1993, the New Mexico Supreme Court reversed the trial court judgment of December 21, 1989 and vacated the jury verdict. Although a motion for rehearing was denied on August 10, 1993, the court modified its disposition and published an Opinion on the same date. Petitioners timely filed a second motion for rehearing under NMSA 1978, SCRA § 12-404(A) which was denied September 23, 1993.

The Court has jurisdiction under 28 U.S.C. § 1257(a).

CONSTITUTIONAL PROVISIONS, STATUTES AND REGULATIONS INVOLVED

United States Constitution, Art. VI, Cl. 2

> This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.

United States Constitution, Amendment V

> No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the Militia, when in actual service in time of War or public danger; nor shall any person be subject for the same offence to be twice put in jeopardy of life or limb; nor shall be

compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation.

United States Constitution, Amendment XIV

Section 1. All persons born or naturalized in the United States, and subject to the jurisdiction thereof, are citizens of the United States and of the State where in they reside. No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.

United States Constitution, Art. IV, § 3, Cl. 2

The Congress shall have Power to dispose of and make all needful Rules and Regulations respecting the Territory or other Property belonging to the United State; and nothing in this Constitution shall be so construed as to Prejudice any Claims of the United States, or of any particular State.

The Mineral Leasing Act of 1920

30 U.S.C. § 181 (excerpt)

Deposits of coal, phosphate, sodium, potassium, oil, oil shale, gilsonite (including all vein-type solid hydrocarbons), or gas, and lands containing such deposits owned by the United States, including those in national forests, but excluding lands acquired under the Appalachian Forest Act, approved March 1, 1911 (36 Stat. 961), and those in incorporated cities,

towns, and villages and in national parks and monuments, those acquired under other Acts subsequent to February 25, 1920, and lands within the naval petroleum and oil-shale reserves, except as hereinafter provided, shall be subject to disposition in the form and manner provided by this chapter to citizens of the United States, or to associations of such citizens, or to any corporation organized under the laws of the United States, or of any State or Territory thereof, or in the case of coal, oil, oil shale, or gas, to municipalities. Citizens of another country, the laws, customs, or regulations of which deny similar or like privileges to citizens or corporations of this country, shall not by stock ownership, stock holding, or stock control, own any interest in any lease acquired under the provisions of this chapter. . . .

30 U.S.C. § 187

No lease issued under the authority of this chapter shall be assigned or sublet, except with the consent of the Secretary of the Interior. The lessee may, in the discretion of the Secretary of the Interior, be permitted at any time to make written relinquishment of all rights under such a lease, and upon acceptance thereof be thereby relieved of all future obligations under said lease, and may with like consent surrender any legal subdivision of the area included within the lease. Each lease shall contain provisions for the purpose of insuring the exercise of reasonable diligence, skill, and care in the operation of said property; a provision that such rules for the safety and welfare of the miners and for the prevention of undue waste as may be prescribed by said Secretary shall be observed, including a restriction of the workday to not exceeding

eight hours in any one day for underground workers except in cases of emergency; provisions prohibiting the employment of any child under the age of sixteen in any mine below the surface; provisions securing the workmen complete freedom of purchase; provision requiring the payment of wages at least twice a month in lawful money of the United States, and providing proper rules and regulations to insure the fair and just weighing or measurement of the coal mined by each miner, and such other provisions as he may deem necessary to insure the sale of the production of such leased lands to the United States and to the public at reasonable prices, for the protection of the interests of the United States, for the prevention of monopoly, and for the safeguarding of the public welfare. None of such provisions shall be in conflict with the laws of the State in which the leased property is situated.

30 U.S.C. § 189

The Secretary of the Interior is authorized to prescribe necessary and proper rules and regulations and to do any and all things necessary to carry out and accomplish the purposes of this chapter, also to fix and determine the boundary lines of any structure, or oil or gas field, for the purposes of this chapter. Nothing in this chapter shall be construed or held to affect the rights of the States or other local authority to exercise any rights which they may have, including the right to levy and collect taxes upon improvements, output of mines, or other rights, property, or assets of any lessee of the United States.

30 U.S.C. § 281

The Secretary of the Interior is hereby authorized, under such rules and regulations as he may prescribe, to grant to any qualified applicant a prospecting permit which shall give the exclusive right to prospect for chlorides, sulphates, carbonates, borates, silicates, or nitrates of potassium in lands belonging to the United States for a period of not exceeding two years: *Provided*, That the area to be included in such a permit shall not exceed two thousand five hundred and sixty acres of land in reasonably compact form: *Provided further*, That the prospecting provisions of this subchapter shall not apply to lands and deposits in or adjacent to Searles Lake, California, which lands may be leased by the Secretary of the Interior under the terms and provisions of this subchapter.

30 U.S.C. § 282

Upon showing to the satisfaction of the Secretary of the Interior that valuable deposits of one of the substances enumerated in this subchapter has been discovered by the permittee within the area covered by his permit, and that such land is chiefly valuable therefor, the permittee shall be entitled to a lease for any or all of the land embraced in the prospecting permit, at a royalty of not less than 2 per centum of the quantity or gross value of the output of potassium compounds and other related products, except sodium, at the point of shipment to market, such lease to be taken in compact form by legal subdivisions of the public land surveys, or if the land be not surveyed, by survey executed at the cost of the permittee in accordance

with regulations prescribed by the Secretary of the Interior.

43 CFR § 3590.0-5(h)

§ 3590.0-5 **Definitions.**

(h) *Ultimate maximum recovery* means that all portions of a leased Federal mineral deposit shall be mined, based on standard industry operating practices. The requirement to achieve ultimate maximum recovery does not in any way restrict the authorized officer's authority to ensure the conservative [sic, i.e., conservation] of the mineral resource and protection of the other resources.

43 CFR § 3594.1

§ 3594.1 **Ultimate maximum recovery.**

(a) Mining operations shall be conducted in a manner to yield the ultimate maximum recovery of the mineral deposits, consistent with the protection and use of other natural resources and the protection and preservation of the environment – land, water and air. All shafts, main exits and passageways, as well as overlying beds or mineral deposits that at a future date may be of economic importance, shall be protected by adequate pillars in the deposit being worked or by such other means as approved by the authorized officer.

(b) New geologic information obtained during the mining regarding any mineral deposits on the lease shall be fully recorded and a copy of the record furnished to the authorized officer, if requested.

STATEMENT OF THE CASE

1. The Mineral Leasing Act of 1920, 30 U.S.C. 181 *et seq.*, establishes a partnership between the federal government and private enterprise for the prudent exploitation and protection of certain mineral resources of the United States including potash. Under the Act the Secretary of the Interior rewards discoverers of deposits of minerals on the public lands with exploration and development rights in return for stated royalties based on gross revenues or gross production to be paid on extraction and sale of listed mineral products. Leases under the Act must include provisions "insuring the exercise of reasonable diligence, skill and care in the operation of said property" and for "the prevention of undue waste." 30 U.S.C. § 187.

As explained in *Boesche v. Udall*, 373 U.S. 472, 477-78 (1963), the United States retains ownership of these lands and the ore they contain. Accordingly the United States has direct interest in the proper, prudent, and orderly extraction of the minerals:

> Unlike a land patent, which divests the Government of title, Congress under the Mineral Leasing Act has not only reserved to the United States a fee interest in the leased land, but has also subjected the lease to exacting restrictions and continuing supervision by the Secretary. Thus, assignments and subleases must be approved by the Secretary, 30 U.S.C. § 187 . . . and he may prescribe, as he has, rules and regulations governing in minute detail all facets of the working of the land, 30 U.S.C. § 189, 30 CFR pt. 221.

These regulations promote prudent operation of mining on public lands by requiring "ultimate maximum recovery," 43 CFR § 3594.1 (*and see* Appendix N, the text of the regulation when the operations began).

2. The leasing program has produced royalties to the Interior Department through 1991 of $2,639,051,177 for coal and other products which might be highgraded (*i.e.*, all listed minerals except oil and gas).[1] Highgrading is "stealing ore" by removal of the best ore first, rendering remaining ore commercially unrecoverable. Black's Law Dictionary (5th ed.), at 655; Finding nos. 58, 59 and 60, Appendix M.

In 1991 alone, total royalties to the Interior Department for coal and other products under the program were $363,180,913. The sales value on which these royalties were paid was $4,116,779,124. Of these totals, New Mexico accounted for $493,316,000 in 1991, of which $32,681,858 was paid to the Secretary as royalty. MMS, *supra*, at 57 and 63.

Private or overriding royalty holders have an interest in enforcing prudent mining standards identical to that of the United States.[2] Private actions to enforce those standards are a necessary and integral part of the scheme

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[1] Minerals Management Service, Royalty Management Program, Mineral Revenues 1991, page 63.

[2] Overriding royalty as defined in the ruling below is "a royalty carved out of a working interest created by an oil, gas or mining lease" and usually involves, as here, the transfer of a lease in which the lessee-assignor retains an interest in production in the form of an overriding royalty. In this case, as is common, Petitioners retained reversionary rights.

under the Mineral Leasing Act and private royalty holders play a significant role in preventing mining waste. (According to the Bureau of Land Management, Southwest Regional Office, Santa Fe, nearly half the leases issued under the Act in New Mexico carry with them overriding royalties to private persons through assignments approved by the Secretary under 30 U.S.C. 187.)

3. Petitioners' predecessor Walter Cross discovered a vast potash deposit on federal BLM land in Lea County, New Mexico and was awarded the right under the Act to prove up and acquire leases on the lands. 30 U.S.C. §§ 281 and 282. He assigned this right to closely held family corporations, the Petitioners. In turn, Petitioners assigned to defendants' predecessor Freeport Sulphur Company, a world-wide mining conglomerate, in exchange for a percentage of net profits as royalty, their sole consideration. All assignments were approved by the Secretary. Each lease issued to Freeport pursuant to the contract of assignment contained the following due diligence provision:

> (k) *Diligence. Prevention of Waste. Health and Safety of Workmen.* To develop and produce in commercial quantities, with ***reasonable diligence, skill and care in the operation of the property,*** the potassium and other mineral deposits susceptible of such production in the lands covered hereby; to carry out, at the expense of the lessees, all reasonable orders of the Secretary, or his authorized representatives (Regional Mining Supervisors, Geological Survey), issued in pursuance of the operating regulations; ***to carry on all mining, reducing,***

> ***refining, and other operations in accordance with approved methods and practice and in conformity with the operating regulations*** to the satisfaction of said representative; ***to take all reasonable precaution to prevent damage to mineral deposits,*** injury to life, health, or property, or ***economic waste;*** . . . .

Trial Exhibit 6, Appendix I.

Freeport obligated itself to comply with this lease provision in the base 1948 agreement between the parties:

> Freeport shall agree to use reasonable diligence and care in exploiting the deposit and all parties agree to use reasonable diligence and care to keep the leases in good standing and to comply with all Federal and State regulations pertaining to potash.

Trial Exhibit 1, Appendix G; Finding no. 15, Appendix M.

In a subsequent agreement in 1951, Freeport obligated itself once again:

> . . . *Subject to the requirements of the leases,* the nature and extent of all exploration, development and mining operations and the time and manner of performing the same shall be as FREEPORT in its sole judgement and discretion shall determine. . . . (emphasis added)

Trial Exhibit 3, Appendix H; Finding no. 15, Appendix M.

Freeport commenced mining in 1957 and stopped operations in 1982. Toward the end of that period, Freeport highgraded the mine.

By highgrading, Freeport ruined the Government's and Petitioners' reversion under the leases amounting to two-thirds of the reserve, some 5,000,000 product tons worth $380,000,000 at time of shut down in 1982, with a royalty value to Petitioners of over $1.8 million. Finding No. 59, Appendix M.

4. On February 3, 1982, Petitioners filed suit in State district court for Santa Fe County, New Mexico. At trial in 1989, a twelve-person jury found that Freeport had breached the contract by highgrading. The jury awarded $1,816,690.23 in compensatory damages based on the royalty value of the unrecoverable ore remaining in the reserve plus $3,000,000 punitive damages, having found highgrading was imprudent. Findings Nos. 59 & 60, Appendix M.

At trial, Petitioners introduced the federal statute, leases, and mining regulations which were accepted into evidence without objection. The trial court instructed the jury that the federal leases and regulations were part of the parties' contract and read them the ultimate maximum recovery regulation in 30 CFR 231.13, again without objection. Appendix J.

The parties agreed at trial to refer affirmative defenses to the trial court for decision. The trial court denied the defenses and issued findings of fact and conclusions of law which corroborated the jury's verdict that Freeport had committed waste by highgrading and other breaches and that Petitioners were damaged in an amount in excess of $1,816,690.23, the jury's compensatory award. Appendices L and M.

5. The state court's modified Opinion of August 10, 1993, reversed the judgment and vacated the jury verdict. Although the Opinion (at A8) acknowledges that the "relevant federal . . . statutes, rules and regulations were incorporated by reference" into the contract of assignment, it does not consider any of these laws or regulations when discussing the extent of discretion and control conferred on Freeport and instead characterizes Freeport's control as unlimited.

Contrary to express findings of the trial court (Appendix M, Nos. 58, 59 and 60), the Opinion dismisses the waste claim on the theory that highgrading benefitted the royalty holders:

> In fact, it could be said that high-grading was in furtherance of the royalty holders' interests. The aim of high-grading as the plaintiffs admitted is profits, albeit short-term profits. As long as the defendants were seeking profits, that was beneficial for the royalty holders and in furtherance of their interests. Any resulting inconvenience in the retrieval of the remaining ore might constitute waste, but that would be actionable only by the lessor, not the holders of an overriding royalty interest. (at A38, 39)

This statement does not consider harm to Petitioners' reversion or the meaning of waste in the federal regulations and is contrary to the jury's and trial court's findings based on federal laws and regulations. Moreover, footnote 6 of the Opinion acknowledges that highgrading damages were the basis for the jury's calculation of compensatory damages. See, Appendix M, Finding 79. Thus, dismissal of the highgrading claim was essential for the state court's ultimate disposition.

Furthermore, in suggesting that waste is not actionable by a net profits overriding royalty holder, the court below appeared to rely on this principle:

> The owner of an overriding royalty is not entitled to the benefit of the covenants of the base lease, express or implied, *in the absence of an express provision in the instrument creating the overriding royalty*. (emphasis added)

(Opinion, at 81) Yet in citing this principle, the Court ignored that here there *was* an express provision in the assignment agreement. *See* Appendices G and H.

In short, at no point did the court below consider the effect of its interpretation of state law on the Mineral Leasing Program under which this dispute arose, even though federal law was pled and tried.

HOW THE ISSUES WERE PRESERVED

The state supreme court's failure to give effect to the parties' written contract could not have been foreseen. Until April 22, 1993, there was no reason to believe that the New Mexico standard of interpretation of the contract diverged from the federal construction that highgrading is "waste," *Dawn Mining Co. v. Watt*, 543 F. Supp. 841, at 843 (D.C.D.C. 1982), *affirmed* 704 F.2d 1293 (D.C. Cir. 1983). No one challenged application of the Mineral Leasing Act to the contract. The Act and regulations were pled in the amended complaint, admitted in the answer, portions were read to the jury (TR 197 *et seq.*) and included in unobjected jury instructions (Appendix J). The pretrial order further preserved the issue whether the contract

was breached by violation of the federal leases. (Appendix K)

The precise questions presented here were preserved in Petitioners' motions for rehearing (Appendices C, D, E, F).[3]

REASONS FOR GRANTING THE WRIT

1. By prohibiting assignors of mining rights under 30 U.S.C. § 187 from enforcing federal anti-waste provisos incorporated into the contract of assignment and by failing to apply federal interpretation of those provisos, the New Mexico Supreme Court has breached the Supremacy Clause, Art. VI, Cl. 2, of the United States Constitution. States may not hinder achievement of the purposes and goals of the Mineral Leasing Act in this way. In *Ventura County v. Gulf Oil Corp.*, 601 F.2d 1080 (9th Cir. 1979), *affirmed* 445 U.S. 947 (1980), the Ninth Circuit Court of Appeals held that county zoning laws and permit requirements could not be imposed on a lessee of oil and gas leases issued by the Secretary under the Mineral Leasing Act, 30 U.S.C. §§ 187, 189. Citing *Kleppe v. New Mexico*, 426 U.S. 529 (1976), the *Ventura* court stated:

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[3] Certiorari may properly be granted where the federal question appears in an unexpected, surprise decision of the state's highest court. *Brinkerhoff-Faris Trust & Sav. Co. v. Hill*, 281 U.S. 673, 677-78 (1930); *Herndon v. Georgia*, 295 U.S. 441 (1935); *Missouri ex rel. Missouri Ins. Co. v. Gehner*, 281 U.S. 313 (1930); *Great Northern Ry. Co. v. Sunburst Oil & Refin. Co.*, 287 U.S. 358 (1932); Stern, Gressman & Shapiro, *Supreme Court Practice* (6th ed. 1986), at 156; 12 Moore's Federal Practice, § 510.11.

> Like *Kleppe*, our case involves a power struggle between local and federal governments concerning appropriate use of the public lands. That the New Mexico authorities wished to engage in activity that Congress prohibited, while the Ventura authorities wish to regulate conduct which Congress has authorized is a distinction without a legal difference.

The court in *Ventura* went on to hold that:

> "Under the circumstances of this particular case, (the local ordinances) stand as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." (*Hines v. Davidowitz* (1941) 312 U.S. 52, 67. . . . *Accord, Jones v. Rath Packing Co.*, (1977) 430 U.S. 519, 526 . . . *Kleppe v. New Mexico, supra*, 426 U.S. at 543.)

As in *Ventura, supra*, at 1084, "the conflict in the present case strikes at the heart of the federal regulation. The Mineral Leasing Act and extensive permit procedures are designed for the very purpose of circumscribing the conditions under which the Government lessee will operate." In the instant matter, those conditions include the leases themselves, which require "due diligence"; and a federal regulation expressly requiring that "mining operations shall be conducted in a manner to yield ultimate maximum recovery of the mineral deposits. . . . " 30 CFR § 231.13, Appendix O, now 43 CFR § 3594.1, and *see* 43 CFR § 3590.0-5(h) (Ultimate maximum recovery means that all portions of a leased Federal mineral deposit shall be mined, based on standard industry operating practices.) Based on substantial evidence, the jury and trial court found that waste through highgrading had occurred. Appendix L and Appendix M, nos. 58 and 59,

Appendix Q. Yet the New Mexico Supreme Court's Opinion encourages waste by failing to give the findings or the regulations on which they were based effect, even though the regulations were expressly made applicable in the contract of assignment.

The state court erred in applying a state rule of decision to determine whether Respondents' highgrading constituted waste under an assignment expressly incorporating federal anti-waste law. The meaning of the federal regulation and required lease language (specifically, whether they prohibit highgrading) is a question of federal law because it touches issues at the core of federal policy. *Wallis v. Pan American Petroleum Corp.*, 384 U.S. 63 (1966); *Western Airlines, Inc. v. Board of Equalization*, 480 U.S. 123, 129 (1987) ("Absent a clear indication to the contrary, the meaning of words in a federal statute is a question of federal law"); *see also Free v. Bland*, 369 U.S. 663, 669-70 (1962) (the Supremacy Clause requires a state court to apply federal law when interpreting the nature of rights and obligations created by federal savings bonds).

Federal law would provide the rule of decision even if Respondents' obligations under the lease and assignment did not require construction of specific terminology in the Act and regulation because uniform interpretation of waste under private contracts of assignment under the Mineral Leasing Act is essential to the "accomplishment and execution of the full purposes and objectives of Congress." *Hines v. Davidowitz, supra.*[4]

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[4] Nothing in 30 U.S.C. § 187 authorizes a court to apply state law in construing the meaning and scope of provisions in a

As held in *Lowey v. Watt*, 684 F.2d 957, 965 (D.C.Cir. 1982):

> Although federal law does not govern all questions of contract interpretation involving leases issued under the Mineral Leasing Act of 1920 . . . it applies to questions of significant implications for federal policy and which require uniform resolution throughout the federal system. . . .
>
> Were state law to govern that question, it would "lead to great diversity in results by making identical transactions subject to the vagaries of the laws of the several states," and it would "subject the rights and duties of the United States to exceptional uncertainty." *Clearfield Trust Co. v. United States*, 318 U.S. 363, at 367. . . .

And see, Mississippi Band of Choctaw Indians v. Holyfield, 490 U.S. 30, 43 (1989) (Congress intended "domicile" to be a matter of federal law to achieve uniformity under Indian Child Welfare Act).

Indeed federal common law governs any question where there is a "significant conflict between a federal policy or interest and the use of state law". *Wallis, supra*, at 68 (a case arising under the Mineral Leasing Act of 1920).

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lease, particularly those provisions which are explicitly required to be included by the Statute and accompanying regulations. The proviso at end of § 187 "assures only that the Secretary of the Interior shall observe state standards in drafting the lease's terms. It is not a recognition of concurrent state jurisdiction." *Ventura, supra*, 601 F.2d at 1085. Similarly, 30 U.S.C. § 189 does not authorize a court to construe a statutory term enacted by Congress against the construction adopted by federal courts. *Ventura, supra*, at 1086; *Dawn Mining, supra*.

Federal interests are frustrated where state law sanctions mining practices forbidden by federal law that damage federal mineral deposits. Such laws reduce the value of the public lands and result in diminished royalty to the federal government and the states. At the same time, they deprive the public of the economic and other benefits of the mineral products whose recovery is promoted in the Act. The effect is to place an obstacle in the path of federal objectives. *See, Ramah Navajo School Board, Inc. v. Bureau of Revenue of New Mexico,* 458 U.S. 832, 845 (1982).

2. By failing to recognize a private cause of action for highgrading, the New Mexico Supreme Court refused to give effect to the incorporated federal regulations and thus undermined the federal scheme. If not reversed, the Opinion will erode federal and common law prohibitions against highgrading and other wasteful practices found by the jury in this case and encourage violation of federal mining regulations by others. *See, e.g., Brewster v. Lanyon Zinc Co.,* 140 Fed. 801 (8th Cir. 1905); *Darr v. Eldridge,* 66 N.M. 260, 346 P.2d 1041, 77 A.L.R.2d 1052 (1959); and *Libby v. DeBaca,* 51 N.M. 95, 179 P.2d 263 (1947) (all of which adopt a common standard for determining imprudent mining).

To our knowledge, no court – federal or state – has ever held that highgrading is "beneficial." The very definition of highgrading is "stealing ore." Black's Law Dictionary (5th ed.) at 655. The notion of beneficial highgrading is an oxymoron.

Unless reversed, the ruling will make it harder for the federal government to achieve the purposes of the

Mineral Leasing Act. Partnerships with private enterprise envisioned in the act will be undermined because private contract rights created under the Act will no longer be governed by uniform federal law. *Lowey v. Watt, supra.* What is waste in one state may not be waste in another.

Dawn Mining, supra, illustrates what is at stake. There a mining company challenged a lease cancellation ordered by the Secretary of the Interior because the company wanted to abandon a low grade pit in favor of a high grade pit in a uranium mine on an Indian reservation. The same regulations involved here governed the lease there. Said the Court, 543 F. Supp. at 843:

> Low grade ore is largely useless unless high-grade ore is available with which it may be blended. . . . The Secretary was therefore entirely justified in concluding, as he did . . . that Dawn "has every motivation to high grade and gut the mine rather than manage it and plan for its long range future." If allowed to proceed Dawn may well deplete the one high-grade pit, leaving the Indian tribe with the worthless low-grade pit. This is serious and irreparable damage.

By introducing the novel concept of beneficial highgrading, the instant ruling directly endangers the mineral leasing program and "significantly conflicts with a federal policy or interest". *Wallis, supra,* at 68.

3. If allowed to stand, the decision in this case will have a significant adverse impact on federal revenues from Mineral Leasing Act leases. Here highgrading ruined a reversion worth $380,000,000 in 1982 prices and caused at least $1,816,690.23 in damages to Petitioners.

Based on a 2% federal gross royalty, the waste cost the federal government at least $7.6 million in future royalty revenue. 30 U.S.C. § 282. *See* Finding no. 59, Appendix M.

In 1991 alone royalties paid to the Secretary under the Act were a third of a billion dollars on highgradeable coal and other products. If only 1% of this income stream were jeopardized by the Opinion below, the loss to the Treasury will be tens of millions of dollars annually. Even if the ruling were not adopted elsewhere, the effect on New Mexico-generated royalties alone would be sizeable. In 1991 New Mexico leases under the Act paid $32.6 million in royalties to the Secretary. Private enforcement suits for breach of proper mining practices have historically been critical in the development of mining law. *See, e.g., Brewster v. Lanyon Zinc, supra,* and its extensive progeny. Relaxing mining principles laid down in that case and others will hurt the Treasury and deprive the public of significant economic and other benefits of ultimate maximum recovery of mineral resources.

Additionally, major revisions of the General Mining Law of 1872, 30 U.S.C. §§ 21 et seq., have recently passed both houses of Congress. S. 775 and H.R. 322. The Senate version imposes federal royalties based on net profits. ***The revenue losses for the federal government will be magnified manyfold if the law to revise the 1872 act and impose higher royalties on mining companies that extract "hard rock minerals" from public lands is passed and the decision below is allowed to stand.*** *Conferees will meet in the coming weeks to resolve the differences. The New Mexico ruling would compromise the new scheme from the outset by its principle that as to a net profits royalty holder highgrading is beneficial.*

4. By erroneously applying state law to reach a contrary result, the New Mexico Supreme Court in violation of the Due Process Clause ignored explicit findings supported by substantial evidence that Respondent's highgrading practice constituted waste. The state court flatly misstates the uncontroverted record when it says (at A39), "it is beyond question that the parties left the mining operations within the sole discretion of the defendants." Both the 1948 and 1951 agreements specifically and expressly bind Respondents to comply with the federal leases assigned to them and with their accompanying regulations. Both the jury and the trial court found these provisions to be part of the parties' contract and indeed this finding was not attacked.

In addition, the New Mexico Supreme Court went against *all* the evidence and express trial court findings when it "found" (at A23) that Petitioners had access to potash prices. Appendices C, D, E, F, and M, nos. 48, 49 and 50. It also ignores trial court findings of misrepresentation as to the basis for the 1968 shutdown and reason for not surrendering the leases. Appendix M, No. 38; Appendix P. And it rules against Petitioner on legal grounds conceded at trial by Respondents. *See* Appendix R (Respondents' requested jury instructions).

The New Mexico Supreme Court makes clear that the jury's highgrading verdict alone sustains the judgment. Therefore there are no independent state grounds which dispose of the matter. Appendix M, Finding 79. In any case, the New Mexico court's disregard of findings may be reviewed by this court. In its entirety, the state court's opinion when viewed from the standpoint of the evidence in this case is a subterfuge to deny federal rights or

benefits to Petitioners. As such it is open to review and should be reviewed because of its adverse impact on the mineral leasing program. *See New York Times v. Sullivan*, 376 U.S. 254, 285 (1964) (the Supreme Court may determine whether governing rules of federal law have been applied correctly to the facts); Wright, Cooper & Gressman, *Federal Practice & Procedure* (1977 ed.), § 4033, at 75, and cases cited therein.

CONCLUSION

The ruling below significantly impedes administration of the Mineral Leasing Program (*see, e.g., United States v. Ruzicka*, 329 U.S. 287 (1946)) and stands as a "serious hindrance to effective administration of the law" (*Rothensies v. Electric Storage Battery Co.*, 329 U.S. 296 (1946)) with specific impact on "the utilization of the public lands." *United States v. Coleman*, 390 U.S. 599, 601 (1968). Further, the ruling below is at odds with well-established construction of the Mineral Leasing Act by the Secretary of the Interior who is charged with the Act's enforcement. *Morton v. Ruiz*, 415 U.S. 199, 201-202 (1974). And federal revenues are affected, a significant reason for granting the petition. *United States v. Mitchell*, 463 U.S. 206, 211, n. 7 (1983). *See, generally*, Stern, Gressman & Shapiro, *supra*, at 216. Further its misstatement of facts and law raises issues of due process in a context of significant federal interest.

We respectfully suggest that the view of the United States be solicited.

The Petition for Writ of Certiorari should be granted.

Respectfully submitted,

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APPENDIX A

Opinion *Continental Potash, Inc. v. Freeport-McMoran, Inc.*, ___ N.M. ___, 858 P.2d 66 (1993) (August 10, 1993)

CONTINENTAL POTASH, INC., et al., Plaintiffs-Appellees and Cross-Appellants.

FREEPORT-McMORAN, INC., et al., Defendants-Appellants and Cross-Appellees.

No. 19054.

Supreme Court of New Mexico.

Aug. 10, 1993.

Holders of overriding royalty interest brought action against mine operators that had been assigned mineral leases, alleging breach of contract and fraud. The District Court Santa Fe County, Petra Jimenez Maes, D.J., entered judgment in favor of royalty holders, and operators appealed. The Supreme Court, Frost, J., held that: (1) applying doctrine of equitable estoppel to toll six-year statute of limitations on breach of contract claim was abuse of discretion; (2) fraud claim was barred by limitations; (3) express contractual provision superseded any implied obligation regarding operation of mine; and (4) operators' practice of mining only high grade ore did not violate implied covenant of good faith and fair dealing.

Reversed.

* * *

Montgomery & Andrews, John B. Pound, Santa Fe, for appellants and cross-appellees.

Roth, VanAmberg, Gross, Rogers & Ortiz, Michael P. Gross, Raymond Z. Ortiz, Santa Fe, for appellees and cross-appellants.

OPINION

FROST, Justice

The motion for rehearing filed in this matter is denied. The decision initially filed in this case is vacated and this opinion is substituted therefore.

Plaintiffs brought this breach of contract and fraud lawsuit in 1982 to recover lost royalty payments, and the jury found for the plaintiffs. Defendants asserted that the plaintiffs' claims were barred by the relevant statutes of limitations and by the doctrines of estoppel and laches. The trial court, however, denied the defendants' motion for summary judgment on these issues.[1] Defendants also moved for a directed verdict at the close of the plaintiffs' case, renewed the motion at the close of all evidence, and moved for judgment notwithstanding the verdict, all of which were denied. In these motions, the defendants primarily claimed that no implied covenants existed, which the jury found the defendants had breached. We

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[1] The court granted defendants' motion for summary judgment on the claim concerning its amortization of assets of the Lea County mine and on a RICO claim.

conclude that the trial court erred on the statute of limitations issue and in submitting the issue of implied covenants to the jury. Accordingly, we reverse the trial court and vacate the jury's verdict.

I. *PROCEDURAL HISTORY*

This case arose from agreements made in 1948, 1949, 1951, 1953, and 1956 between the plaintiffs, Continental Potash Company (Continental) and Kansas City Testing Laboratories, Inc. (KCTL), later known as Cross Laboratories, Inc., and the defendants, Freeport Sulphur Company, predecessor to the named defendants Freeport-McMoran, Inc. and Freeport Minerals Company (Freeport), and National Potash Company (National). The agreements granted Freeport the right to explore commercial potash deposits with an option to acquire mining rights through assignment of certain prospecting permits and leases that the plaintiffs held on lands located in southeastern New Mexico. In the assignment of the leases to Freeport, the plaintiffs reserved an overriding royalty interest[2] in the net profits derived from the mining operation.

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[2] The term "overriding royalty" is used to describe a royalty carved out of a working interest created by an oil, gas, or mining lease. 2 Howard R. Williams & Charles J. Meyers, *Oil and Gas Law* § 418, at 344 (1992). Usually, the reservation of an override involves the transfer of a lease in which the lessee-assignor (in this case the plaintiffs) retains an interest in production in the form of an overriding royalty. The overriding royalty interest is an interest free of the expenses of production. 2 *id* § 418.1, at 345. It is a nonpossessory interest in land. 2 *id.* § 418.1, at 347.

In a 1982 lawsuit, the plaintiffs alleged that the mining operation conducted by the defendants during the periods 1956-1968 and 1976-1982 should have resulted in substantial net profits instead of accumulating a $16 million net loss. Thus, the plaintiffs alleged that they suffered loss of royalties due to the defendants' breach of contract and fraud in the operation of the mine.

The issues of breach of contract and fraud were tried to a jury, but the parties stipulated that the district court would be the fact finder on all issues concerning the affirmative defenses. The jury returned a verdict in favor of the plaintiffs for breach of implied covenants and fraud. The district court then denied all of the affirmative defenses as a matter of law, finding that the statutes of limitations were tolled by the doctrine of equitable estoppel. The court based its application of the doctrine of equitable estoppel upon its finding that the defendants had fraudulently concealed from the plaintiffs the facts upon which they could have based their lawsuit within the respective limitations periods. The court further concluded that substantial evidence supported each of the jury's express and implicit findings underlying the fraudulent concealment issue.

II. *ISSUES*

The legal questions presented on appeal are whether the trial court was incorrect (1) to toll the six-year statute of limitations on the contract claims and the four-year statute of limitations on the fraud claim; and (2) to find implied covenants governing the defendants' conduct, which the defendants allege were inconsistent with the

express terms of the written agreements. In addition, National challenges the award of compensatory damages ($1,816,690.23) and punitive damages ($3,000,000), and it contends that the court erred by permitting the plaintiffs to recover on the claim of a nonparty, Mary Borders Byrte. National also claims that the trial court should not have submitted the fraud issue to the jury. Because we hold that the district court erred in denying defendants' motion for directed verdict on the statute of limitations issue and in implying and enforcing contractual obligations against the defendants beyond the duties in the written agreements, it is unnecessary to address the other issues raised on appeal and on cross-appeal

III. *FACTS*

A. *The Parties*

In the 1940s, Walter M. Cross, the original prospector on the lands, discovered a potash deposit in southeastern New Mexico. Cross and members of his family obtained prospecting permits and leases from the federal and state governments for discovering the ore body. Shortly thereafter, Cross incorporated Continental for the purpose of developing the ore body and assigned part of his interest in the mineral rights to Continental. Cross also assigned part of his interest in the same mineral rights to KCTL, another closely held corporation.

At about the same time, Freeport was prospecting for potash deposits in the same general area, which led to negotiations between KCTL, Continental, and Freeport about the possibility of Freeport developing both ore

bodies. Negotiations resulted in the formation of a contract that was initiated by a letter agreement in 1948 and that was subsequently modified and supplemented in more formal documents in 1949, 1951, 1953, and 1956. In 1948 and 1949, the plaintiffs granted Freeport the right to explore for potash on land in Lea County, New Mexico with the option of receiving assignment of the prospecting permits and mine leases issued by the United States government and the State of New Mexico. In 1951, after initial exploration and completion of the prospecting work, KCTL and Freeport executed another agreement covering two additional mining permits with terms substantially the same as those in the 1949 agreement. Freeport exercised its option for assignment of the permits and leases.

Thus, as of the early 1950s, Freeport was the lessee of the subject mining lands, and the United States and the State of New Mexico were the lessors. KCTL and Continental held overriding royalty interests. KCTL was under the control of Walter Cross until his death in 1954, and Continental had been sold to a group of investors headed by Milton McGreevy.[3] With the consent of the federal and state governments, Freeport assigned its rights as lessee in the potash leases to National in 1955. National was a corporation equally owned by Consolidation Coal Company and Freeport, and it was created for the purpose of developing the Lea County potash deposits.

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[3] The district court found Cross to be a well-educated, sophisticated businessman and inventor. McGreevy was a sophisticated and knowledgeable businessman as well. He was an original shareholder of Continental.

B. *The Arrangement for Payment of Royalties.*

Freeport had agreed to pay KCTL and Continental a royalty of eight percent of the divisible profits from the production and marketing of the mined potash. Sometime after the McGreevy group purchased Continental, a dispute arose between Continental and KCTL concerning their respective royalty rights. The dispute was resolved in 1956 in an agreement between the plaintiffs and National to pool all royalty interests, thus merging fractional holdings into a unified whole. The 1956 agreement expressly superseded previous royalty provisions and granted the plaintiffs a cumulative net profit royalty. Payment of royalties, however, was conditioned upon realizing a net profit during each fiscal year. Under this arrangement, whenever National was in a net profit posture, all royalty holders would receive payment without regard to whose potash was being mined, milled, and sold.

The net profits royalty provisions also included what the parties called a "net loss carry-forward," which meant that if National began production on the mining lands, it was required to pay a net profit royalty in any given fiscal year only if the net loss that had accumulated prior to that year had been overcome. By reserving a net profit royalty instead of a smaller gross receipts royalty, the plaintiffs were tied to the profitability of the plaintiffs were tied to the profitability of the mine rather than to its gross output, a fact that became pivotal when the mining operation later proved to be unprofitable.

C. *Exclusive Control and Discretion by National.*

In addition to the provisions detailed above, the parties agreed that: (1) National could elect to terminate the agreement or to surrender any permit or lease after giving proper notice to the plaintiffs; (2) National could exercise its sole judgment and discretion in determining which extensions of permits or which leases would be applied for; (3) if National failed to instruct the plaintiffs regarding extensions, release to the plaintiffs of any permit or lease would be automatic; (4) National could exercise exclusive control, discretion, and judgment regarding all of its mining operations, and it could determine the quantity of ore mined and the quantity left unmined; and (5) National could elect to suspend operations "for as long as it may determine whenever in its opinion economic conditions or other causes make it desirable so to do." The relevant federal and state statutes, rules, and regulations were incorporated by reference. National also agreed to furnish the royalty holders with periodic financial statements of the results of its operations to be verified by an independent certified public accounting firm and prepared in accordance with generally accepted accounting principles.

D. *Mining Operations.*

National operated the mine from the time it opened in 1956 until 1968 (first run) when operations were temporarily suspended until 1976. Immediately upon opening the mine, it became apparent that the quality of the Lea County ore was not good enough to render it marketable by itself. To produce a saleable product, National

purchased higher grade ore to blend with the lower quality ore.

In 1959 Freeport acquired the right to develop another ore body in Eddy County, New Mexico. The Eddy County mine contained a higher quality ore than the Lea County mine, and National began blending ores from the two mines, which extended the life of both ore deposits. Plaintiffs never owned an interest in the Eddy County mine.

By 1965 most of National's production came from the Eddy County mine. Profits started to decline in 1967, however, and mining operations ceased at the Lea County mine in 1968. Prior to the suspension, National gave the royalty holders notice of discontinuing its mining operations. The plaintiffs never demanded that National surrender or assign the leases to them, and they never claimed that failure to surrender the leases constituted a default under the agreements. With the shutdown of the Lea County mine and production coming solely from the Eddy County mine, the royalty holders did not receive any royalty payments from 1969 to 1973.

When the potash market began to recover in the mid-1970s, National prepared to reopen the Lea County mine. National invested an additional $1.8 million in the Lea County mine and notified the plaintiffs of reopening the mine. The mine had slight production in 1974-75, but not enough to generate a net profit. The mine reopened on a full-scale basis in 1976 and operated until February 1982 (second run). The Eddy County mine was exhausted and closed permanently in 1976. Between 1976 and the closing of the Lea County mine in 1982, National's only

potash production came from the Lea County mine. Due to the unprofitable nature of the mining operation, however, the plaintiffs earned no royalties during this period.

Because National had exhausted its Eddy County mine and apparently had no other source of higher grade ore to blend with the ore from the Lea County mine, National decided to "high-grade" the mine during the second run of production. High-grading is a mining term that entails selectively removing the richer grade ore from a mine. The effect is that the remaining mineral deposit is more expensive to retrieve and often impossible to retrieve commercially within a reasonable time period.

E. *The Agreement Between National and Central Farmers.*

In 1980 and 1981, the price of potash on the export market ballooned and was approximately 30% to 50% higher than National realized from its sales on the domestic market. In their lawsuit, the plaintiffs alleged that National failed to market Lea County potash on the export market in breach of its implied duty to exercise reasonable diligence. Had it done so, they argued, National would have eliminated the accumulated loss carry-forward in two years and generated significant net profits and thus substantial royalties. These lost royalties were valued in excess of $800,000. National could not take advantage of the boom in the Market, however, because it was obligated by an outputs contract.

In December 1958, National entered into a sales agreement with Central Farmers Fertilizer Company

(Central Farmers), in which Central Farmers agreed to buy the entire output of the Lea County mine up to 500,000 tons per year through 1974. Central Farmers was interested in developing a continuous source of potash for re-sale to farm cooperatives across the country. National was interested in finding a steady customer for its potash, believing that a guaranteed ongoing customer would give it an advantage against fluctuations in the potash market. In addition, such an arrangement ensured that National could honor its sizable debt service.[4] The price agreed upon was "market price" less a discount to reflect the fact that National could forego employment of a sales staff to market the ore. The parties established as a benchmark for determining market price the "Carlsbad list price.")[5] Thus, the price National would receive was tied to prices in the local potash market.

National and Central Farmers simultaneously executed a stock purchase and option agreement, giving Central Farmers an option to purchase enough shares in

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[4] Freeport borrowed $12,500,000 from Metropolitan Life Insurance Company and combined with $7,000,000 of its own money, it developed and equipped the Lea County mine. The loan was paid off in 1974.

[5] The Carlsbad list price was the lowest price quoted and published on a given date by one Carlsbad producer and met by another Carlsbad producer. The Carlsbad list price represented the price at which Carlsbad producers were actually selling their potash at the time. By the late 1960s, the Carlsbad list price no longer represented the actual market price of potash, despite continued publication of prices by the Carlsbad producers, because of the influx into the market of foreign potash competitors with lower prices.

National to bring its ownership interest up to 45%. The deadline for exercising the options was June 30, 1969.

In January 1964, Central Farmers and National amended their 1958 agreement by changing the price discounting formula and extending the term of the agreement to June 30, 1980. Six months later, Central Farmers assigned its right to purchase the National stock back to National, released its option to purchase additional shares, and sold the 500 shares it then owned back to National. In July 1964, National and Central Farmers executed another contract in which Central Farmers was given another option to purchase a 45% undivided interest in the mine itself, exercisable for a period of one year after National permanently ceased mining operations. Central Farmers never exercised the option.

F. *Findings by the Jury and the Trial Court.*

The jury found that the defendants failed to act as a reasonably prudent operator and thereby breached implied covenants by (1) failing to blend Lea County ore with Eddy County ore during the second run from 1976 until shut-down; (2) high-grading the Lea County ore; (3) failing to sell Lea County ore at the highest and best price obtainable; (4) failing to account with fidelity and charging the plaintiffs' royalty account with improper charges; and (5) failing to surrender the leases when National ceased operations in 1968. The jury also found that the defendants committed fraud but that no additional damages for fraud should be awarded. The jury awarded the plaintiffs compensatory and punitive damages totaling

$4,816,690.23,[6] with post-judgment interest at the rate of fifteen percent per year from the date of entry.

In support of its finding of fraudulent concealment, the trial court found that the defendants misrepresented or deliberately did not disclose to the plaintiffs: (1) the true marketing scheme in the Central Farmers contract; (2) the true reason for failing to surrender the Lea County leases when the mine was temporarily closed in 1968; (3) the true risks to the plaintiffs in reopening the Lea County mine in 1976 without the benefit of higher grade ore for blending; (4) the true level of overhead allowable to the plaintiffs' royalty account from 1976 to 1982; and (5) the high-grading program.

IV. *DISCUSSION*

A. *Introduction.*

Defendants contend that the trial court erred when it refused to grant their motion for summary judgment based upon the affirmative defenses of the applicable statutes of limitations and the doctrine of laches. The defendants claim that the district court misapplied the doctrine of equitable estoppel to toll the statutes of limitations. The court found that the defendants deliberately failed to disclose material facts to the plaintiffs "on a

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[6] The amount of the plaintiff's compensatory damages was derived from calculations based upon the value of ore left in the ground after the high-grading process. The court found that "the remaining product tons in the ground had a then-market value of approximately $380,000,000 and a reasonable royalty value to the plaintiffs on that date in excess of $1,816,690.23."

regular, continuing and complete basis." The court also concluded that the defendants' silence, misrepresentation, omission, and concealment "constituted fraudulent concealment for purposes of the statute of limitations." To the contrary, the record shows that the plaintiffs expressed detailed concern about their contractual rights, the prospects for payment of royalties, the marketing plan under the Central Farmers contract, and accounting procedures as they pertained to their royalty account. In addition, the defendants had no fiduciary relationship with the plaintiffs and thus no duty to disclose information to them, the breach of which might have constituted fraudulent concealment. They could have filed suit within the relevant time periods.

Regarding the breach of implied covenants, the plaintiffs argue that implied covenants are the bedrock of mining law and are designed for the protection and mutual benefit of both parties. The defendants claim that implied covenants may be found only when they embody the intention of the parties and are necessary to give effect to that intention. In any event, the defendants claim that implied covenants may not exist when express contractual provisions address the same subject matter. We hold that the trial court erred as a matter of law when it enforced implied covenants against the defendants on the issues not barred by the statutes of limitations.

B. *Standard of Review.*

We review the district court's application of equitable estoppel under an abuse of discretion standard. *See Padilla v. Lawrence*, 101 N.M. 556, 562, 685 P.2d 964, 970

(Ct.App.), *cert. denied*, 101 N.M. 419, 683 p.2d 1341 (1984) (decision whether equitable relief should be granted is within the sound discretion of trial court and will not be reversed on appeal unless clear abuse is shown). "An abuse of discretion will be found when the trial court's decision is clearly untenable or contrary to logic and reason." *Newsome v. Farer*, 103 N.M. 415, 420, 708 P.2d 327, 332 (1985). Such discretion is not a mental discretion to be exercised as one pleases, but is a legal discretion to be exercised in conformity with the law. *Sunwest Bank of Albuquerque v. Roderiguez*, 108 N.M. 211, 213, 770 P.2d 533, 535 (1989).

We review the district court's finding of implied covenants according to whether it correctly applied the law to the facts in the case. *Farmers, Inc. v. Dal Machine & Fabricating, Inc.*, 111 N.M. 6, 8, 800 P.2d 1063, 1065 (1990). In addition, we view the district court's findings of fact most favorably for the appellee, indulging all reasonable inferences in its favor, but the conclusions of law must be based upon and supported by the findings of fact. *Id.*

C. *Tolling the Statutes of Limitations – Equitable Estoppel.*

Estoppel precludes one party from asserting a right when another party has relied to his detriment upon the acts or conduct of the first party and when asserting that right would prejudice the other who has acted thereon in reliance. *Garcia v. Garcia (In re Estates of Salas)*, 105 N.M. 472, 475, 734 P.2d 250, 253 (Ct.App. 1987). As we stated in *Capo v. Century Life Insurance Co.*, 94 N.M. 373, 610 P.2d 1202 (1980):

> The essential elements of equitable estoppel as related to the party estopped . . . are: (1) conduct which amounts to a false representation or concealment of material facts, or, at least, which is calculated to convey the impression that facts are otherwise than, and inconsistent with, those which the party subsequently attempts to assert; (2) intention that such conduct shall be acted upon by the other party . . . ; and (3) knowledge, actual or constructive, of the real facts. . . . As related to [the party claiming] estoppel, the essentials are: (1) lack of knowledge and of means of knowledge of the truth as to the facts in question . . . ; (2) reliance upon the conduct of the party estopped . . . ; and (3) action based thereon of such character as to change its position prejudicially.

Id. at 377, 610 P.2d at 1206; *Stuckey's Stores, Inc. v. O'Cheskey*, 93 N.M. 312, 324, 600 P.2d 258, 270 (2979), *appeal dismissed*, 446 U.S. 930, 100 S.Ct. 2145, 64 L.Ed.2d 783 (1980).

We find particularly significant here the requirements of lack of knowledge and the lack of means by which knowledge might be obtained by the party asserting estoppel. *See Garcia*, 105 N.M. at 475, 734 P.2d at 253. In addition, the party asserting estoppel must show that he relied upon conduct, and such reliance must have been reasonable. *C & L Lumber & Supply, Inc. v. Texas Am. Bank/Galeria*, 110 N.M. 291, 297-98, 795 P.2d 502, 508-09 (1990). Equitable estoppel will be applied when the party estopped intends or expects that the innocent party will act on those representations. *Green v. New Mexico Human Servs. Dep't, Income Support Div.*, 107 N.M. 628, 629-30, 762 P.2d 915, 916-17 (Ct.App.1988). So, a party may not claim

estoppel unless there is reasonable reliance upon the acts or conduct of another, and he is induced to take or forgoes from taking a position to his prejudice or detriment, *Capo*, 94 N.M. at 377, 610 P.2d at 1206.

The existence of grounds justifying a claim of equitable estoppel is a question of fact, and the party alleging and relying on such claim has the burden of establishing all facts necessary to prove it. *Garcia*, 105 N.M. at 475, 734 P.2d at 253. In the case of fraudulent concealment, the facts that a party must show are: (1) the use of fraudulent means by the party who raises the bar of the statute; (2) successful concealment from the injured party; and (3) that the party claiming fraudulent concealment did not know or by the exercise of reasonable diligence could not have known that he might have a cause of action. *See Keithley v. St. Joseph's Hosp.*, 102 N.M. 565, 570, 698 P.2d 435, 440 (Ct.App.1984), *cert. quashed*, 102 N.M. 565, 698 P.2d 435 (1985).

The party must plead the circumstances giving rise to estoppel with particularity. *Hardin v. Farris*, 87 N.M. 143, 146, 530 P.2d 407, 410 (Ct.App.1974). Bald allegations of concealment are not sufficient to make out a case of fraudulent concealment. *See* SCRA 1986, 1-009(B) (Repl.Pamp.1992). So, the party asserting estoppel must sustain the burden of showing not only that he failed to discover the cause of action prior to the running of the statute of limitations, but also that he exercised due diligence and that some affirmative act of fraudulent concealment frustrated discovery notwithstanding such diligence. *See Capo*, 94 N.M. at 377, 610 P.2d at 1206; *Keithley*, 102 N.M. at 570, 698 P.2d at 440.

D. *The breach of Contract Claim.*

After thorough and careful review of the record, proceedings, and exhibits, we are compelled to hold that the district court abused its discretion in applying the doctrine of equitable estoppel to toll the six-year statute of limitations on the breach of contract claim. The grounds upon which the plaintiffs based their claims were apparent to them many years prior to filing the 1982 complaint, and they could have commenced the action within the statutory period.[7] The contents of the correspondence generated between the defendants and the plaintiffs throughout the relevant time period reveal the circumstances and details surrounding each fact identified by the trial court as a material fact allegedly concealed from the plaintiffs.

The plaintiffs' allegations pertaining to fraudulent concealment on the breach of contract and fraud claims overlap to some extent. For the most part, however, the plaintiffs point to circumstances surrounding the Central Farmers agreement and the defendants' failure to surrender the leases in 1968 as supporting the trial court's application of equitable estoppel to toll the statute of limitations on the breach of contract claim. Regarding the allegation of fraud, the plaintiffs claim that the defendants' misrepresentations about the prospects for future profits, especially at the beginning of the second run, support the trial court's application of equitable estoppel to toll the statute of limitations on the fraud claim.

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[7] Generally, actions based on written contracts must be brought within six years of an alleged breach. *See* NMSA 1978, § 37-1-3(A) (Repl.Pamp.1990).

1. *The Central Farmers Agreement.*

Plaintiffs theorize that the sales agreement between National and Central Farmers was unreasonably beneficial to Central Farmers and unduly burdensome to National. They contend that the favorable terms for Central Farmers were the result of a less than arms-length relation between the two corporations. The argument is that if National had sold its product on the open market during the period in which it was obligated by the Central Farmers contracts, it would have shown a profit and would have been able to pay royalties to the plaintiffs. The plaintiffs were aware of these facts, however, many years before 1976, which was the inception of the six-year period on the contract claim provided by the statute of limitations.

The record indicates that National made no effort to conceal from the plaintiffs its 1958 contract with Central Farmers. In fact, two weeks after the sales agreement was executed, Continental learned about it. McGreevy expressed his opinion that the sales agreement was not in the normal course of business and might adversely affect National's profits, which in turn could prejudice the royalty holders' interests. The royalty holders complained about the royalty arrangement and sought to amend the contract. In the same month, Wells, an agent of National, answered McGreevy and refused to amend the agreement, stating that the "royalty holders are in the position of sharing not only the profits from mining but also the risk . . . [and that] mining on these leases has resulted in very substantial losses to this company since February 1957, when ore was first mined on them . . . [which] have been a direct result of the vastly inferior quality of the ore

found on these leases compared to other ore presently being mined on a commercial basis in the Carlsbad area."

In a letter dated April 4, 1960, McGreevy complained to his lawyer about the Central Farmers contract:

> In addition it seems to me it is a major item in this situation that [Freeport] sold half their stock in National Potash to a cooperative which means their profits will not be handled on a normal corporation basis and since our royalties are related to the profit, they may have by that action prejudiced our future position.
>
> * * *
>
> *I am wondering if we could go into court* and reconstrue [sic] the whole situation in such a way as to protect our equitable position in that we might be entitled to a fair royalty on a basis of tonnage mined. If we don't do something like that, I am very doubtful as to whether our stockholders will have any kind of a proper recovery for their investment and for their position in this matter. [Emphasis added.]

In November 1960, McGreevy again complained to Wells specifically about the contract with Central Farmers. McGreevy wrote another letter to Wells in January 1962 complaining about the same thing. In the January 1962 letter, the plaintiffs again expressed detailed concerns about the Central Farmers arrangement, the discretion to operate the mine that was granted to the defendants under the agreements, and the alleged accounting inequities. The letter states in part:

> [W]e made some legal investigation . . . and we have not gone to great expense to employ accountants to exhaustively study this situation

> or attorneys to explore it fully, but we did develop some rather strong and persuasive decisions of law . . . that the operator must conduct his operations in such a way as to be fully fair and equitable to the royalty owner. . . .
>
> * * * *
>
> We think that your operations have been without proper regard to our position . . . and that we have enforceable rights to correct this situation. . . . [W]e feel very strongly that under the fiduciary relationship that exists between National Potash and [the royalty interest holders], the former has not only failed to protect the interests of the latter but has subordinated them to what has most suited your company with resultant prejudice to the [royalty interest holders]. This certainly could never have been the purpose of our agreement.

Wells answered in March 1962 and vigorously defended National, advising McGreevy in no uncertain terms that National was not going to renegotiate the contracts or pay a "settlement" to the royalty holders.

By letter of March 1962, the defendants responded in detail to each ground that the plaintiffs addressed, in particular the history of the Lea County mine, the lack of profits, and the reasons for the long-term contract with Central Farmers. Moreover, in a 1963 letter to the plaintiffs, their attorney "summarize[d] the exchange of correspondence and arguments with National Potash Company" and suggested a response. In 1963, one of the royalty interest holders, in summarizing his conversation with one of the defendants' agents, stated:

> the question of a law suit has in fact been mentioned from time to time in discussion among the [royalty interest holders], but none of them would be desirous of taking such course of action if it could be avoided.
>
> Even if legal action was taken, the sentiment would not be one of ill will or anger but rather as a result of a feeling of frustration. It would be the same as if having exhausted all possible avenues of reaching a friendly settlement, there was nothing left but to test the validity of the contract through the Courts. In this connection, the [royalty interest holders] might feel that there was nothing to lose by trying this.

Despite all of this, the plaintiffs waited until 1982 to file a lawsuit alleging breach of contract. Clearly, at least by 1962, plaintiffs were aware of the Central Farmers marketing plan and possessed sufficient knowledge upon which to base a breach of contract action against the defendants.

McGreevy's letters quoted above also indicate an awareness of a possible conflict of interest arising from the agreement between National and Central Farmers. McGreevy specifically addressed the conflicts of interest in a subsequent letter to Wells. The plaintiffs were also aware that National was according multiple discounts to Central Farmers over and above the discount specified in the outputs contract. In addition, the plaintiffs complained that the price structure in the Central Farmers agreement decreased and that they had no way, absent disclosure from National, to discover the true price at which National sold potash to Central Farmers. The

plaintiffs stated that no one outside the potash industry could learn the price of potash. Yet, McGreevy sat on the board of directors of a company that was also in the potash market. Thus, if the plaintiffs were not aware of material facts, McGreevy and the others could have discovered the material facts through exercise of due diligence.

2. *The Failure to Surrender the Leases.*

Any breach of contract or implied covenant for failure to surrender the leases occurred in 1968 at the end of the first run. National contemporaneously notified the plaintiffs of the shut-down, but they failed to demand surrender of the leases. Being aware of the shut-down, the plaintiffs had the option of immediately demanding surrender or filing suit based upon this factor within six years after the 1968 shut-down.

The plaintiffs claim that the true facts surrounding the nonsurrender were not communicated to them, but in fact, they were informed of the mounting losses after 1968. The gravamen of the plaintiffs' lawsuit was to recover royalties that should have resulted from a profitable mining operation. Yet the plaintiffs were aware of the escalating debt from the financial reports from 1968 to 1976, and still they waited until 1982 to file their lawsuit premised upon lost profits due to the nonsurrender of the leases in 1968. This is a classic example of "sitting on one's rights."

3. *The Absence of Fraudulent Concealment.*

As stated above, the plaintiffs were aware of certain material facts upon which to base their breach of contract claim in the early 1960s. Their argument that the defendants misrepresented those facts to them, therefore, fails to support the application of equitable estoppel. In addition to claiming that the defendants affirmatively misrepresented facts to them, the plaintiffs claim that the defendants failed to disclose certain other material facts, which also constituted fraudulent concealment.

To invoke the doctrine of equitable estoppel by silence, the party must first establish that there was a duty to speak, and he must show that the silent party knew that he was relying upon that silence. *Capo*, 94 N.M. at 377, 610 P.2d at 1206. If there is a confidential or fiduciary relationship between the parties, the failure to disclose material facts or the suppression of material facts when required to disclose them, which induces detrimental reliance may constitute fraudulent concealment giving rise to equitable estoppel. *Keithley*, 102 N.M. at 570, 698 P.2d at 440. Absent a fiduciary duty to speak on the part of the defendants, however, silence, nondisclosure, or denials of alleged fraudulent conduct are insufficient to constitute fraudulent concealment so as to toll a statute of limitations. *Capo*, 94 N.M. at 377, 610 P.2d at 1206.

The plaintiffs confuse the issue here by claiming that an implied covenant of good faith, which the trial court found existed, imposed a duty upon National to disclose material information. National's systematic failure to disclose material information in breach of its implied covenant of good faith, the plaintiffs argue, constitutes

fraudulent concealment, thereby tolling the statutes of limitations. The issue of implied covenants in this case, however, goes to whether a breach of contract existed, not to whether National had a duty to disclose material information, the breach of which might have constituted fraudulent concealment. Unlike fiduciary duties, covenants of good faith do not require an exclusive operator to subordinate its interest to that of the royalty holders. *Murdock v. Pure-Lively Energy 1981-A, Ltd.*, 108 N.M. 575, 579, 775 P.2d 1292, 1296 (1989). Even though the defendants owed contractual duties to the plaintiffs and also owed them a duty of good faith and fair dealing, a fiduciary relationship did not automatically arise from these circumstances in which the defendants were essentially handling their own property. *See Garfield v. True Oil Co.*, 667 F.2d 942, 945 (10th Cir.1982). Given the type of agreement at issue here and the legal relationship between the parties, albeit heavily tilted in favor of National, no fiduciary duty existed, and the trial court so found. Without a fiduciary duty, no duty to disclose or speak existed. Thus, silence or failure to disclose certain information to the plaintiffs here could not operate to toll the statutes of limitations.

Notwithstanding our holding that no duty to disclose existed, the record does not demonstrate that throughout the relationship between the parties from 1948 to 1982, the defendants intentionally and deliberately concealed facts with the hope that the plaintiffs would forego bringing legal action. As has been demonstrated, the plaintiffs contemplated legal action in the 1960s predicated upon the Central Farmers agreement, and any issues presented in their 1982 lawsuit based upon nonsurrender were

apparent to them in 1968 when National shut the Lea County mine down, but in any event before 1976. Defendants' conduct and representations, therefore, cannot be characterized as concealing facts material to a determination by the plaintiffs about whether to file suit. The trial court, therefore, erred in applying the doctrine of equitable estoppel in light of the terms of the contract, the duties and obligations attendant thereto, and the knowledge demonstrated by the plaintiffs in the 1960s.

E. *The Fraud Claim.*

The defendants assert that the plaintiffs failed to allege fraud at trial and that their only claim below was for breach of implied covenants. The defendants claim that the trial court confused the issue when it submitted the issue of substantive fraud to the jury when the only issue before the court was whether the defendants were guilty of fraudulent concealment to support the application of equitable estoppel to toll the statute of limitations on the contract claims. Distinguishing fraud from fraudulent concealment, the defendants claim that fraud should not have been an issue in the case at all. The jury found that the defendants committed fraud, however, and the trial court sustained its finding. Accordingly, we will review that decision.

The plaintiffs allege that the defendants committed fraud in operating the Lea County mine and base that claim primarily upon the defendants' representations of the prospects for royalties during the second run of production. As discussed above, however, the plaintiffs demonstrated sufficient knowledge of these issues more than

for years before the complaint was filed in 1982.[8] Consequently, they were time-barred from pursuing a fraud claim on these grounds as well.

1. *Representations about Future Profits.*

The record contains additional statements by Wells, in a November 1956 letter, that can be properly characterized as expressions of opinion and speculation about the mining operation and its relationship to royalties for the plaintiffs. On November 15, 1960, McGreevy expressed in a letter his concerns about the accounting techniques, the relationship between National and Central Farmers, and the lack of profits in 1960. This letter demonstrates an awareness of additional grounds upon which the plaintiffs based their fraud claim.

Again in 1963, at a royalty holders' meeting, it was acknowledged that another deficit from the Lea County mine was possible, but that "no immediate action should be taken on a lawsuit at this time" presumably based upon the plaintiffs' hope that royalties would begin to flow in 1964. Another of the defendants' letters, dated February 1966, candidly expressed the facts that production at the Lea County mine was low, that "[f]urther expansion does not seem likely," and that the level of mineralization from the Lea County mine was "unusually low." A discussion of accounting procedures relating to the Lea County mine was also included in the letter to

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[8] Fraud actions must be brought within four years of the event, NMSA 1978, Section 37-1-4 (Repl.Pamp.1990), or from the time the fraud is discovered Section 37-1-7.

McGreevy. In 1967, the plaintiffs were aware that it "was doubtful that there would be any profit to [the royalty interest holders] for the next two years and perhaps even a slight loss." In that letter, the issue of the defendants' discretion to operate the mine was raised again. After approximately $78,000 was paid in royalties during the mid-1960s, National went into a net loss position that steadily grew during the late 1960s and early 1970s. Most significantly, the plaintiffs had knowledge of the accumulating losses from the annual financial statements that they received from National.

The plaintiffs were notified that the July 1968 shutdown of the Lea County mine was "a result of market condition." in 1968, when National closed the mine, the plaintiffs obviously were aware of the impossibility of realizing a profit from a closed mine. In January 1973, Rothwell, an official of National, wrote McGreevy predicting bad times for the American Potash industry due to intense price competition from Canada, and reminded him that National may never reopen the mine. Rothwell's letter of January 29, 1973, tells McGreevy that the Canadian potash producers were expected to bring down the price of potash to a point where National would not be able to compete. Rothwell said nothing that any reasonable person could read as guaranteeing future net profits, thus lulling the plaintiffs into repose. He certainly said nothing that would give a reasonable person the impression that any future net profit would be large enough or consistent enough to wipe out the then existing accumulated loss. In an August 1974 letter to McGreevy, Wells worded his comments on reopening the mine in conditional terms and stated that the mine might not reopen.

The letter cannot be read as giving a guarantee of sustained, significant profit. Rather, it was more akin to an opinion than to fact, which the plaintiffs confirm by continually referring to the alleged actionable statements by the defendants as "puffing." Fraud cannot be predicated upon the expression of an opinion. *See Agnew v. Landers*, 59 N.M. 54, 66, 278 P.2d 970, 977 (1954).

2. *The plaintiffs' fraud claim was time-barred.*

Any allegation of fraud should have been filed in the late 1960s or early 1970s when the correspondence between the parties demonstrates the plaintiffs' awareness of facts upon which they eventually based their fraud claim, specifically the absence of profits. The 1956 agreement contained no guarantee of a net profit, but it did openly contemplate the possibility of net losses and the accumulation of a growing net loss. It specifically addressed a net loss carry-over arrangement, which clearly meant that no royalty would be paid until the entire accumulation was eliminated, and the plaintiffs indicated that they understood this arrangement. By 1976, with the mine open again and functioning on a full-scale basis, the net loss had grown substantially. The plaintiffs were aware or should have been aware of this from the financial records they received from National from 1975 to 1977. Any cause of action for fraud based upon the facts articulated by the plaintiffs, therefore, clearly arose before 1978, more than four years prior to filing the complaint.

F. *The Breach of Implied Covenants – Blending and High-Grading.*

Our conclusion that the statutes of limitations barred the plaintiffs' contract and fraud claims cannot logically reach two issues: the failure to blend and high-grading during the second run of production. Because the second run did not begin until 1976, the plaintiffs' contractual claims concerning blending and high-grading necessarily fall within the six-year limitations period. In addition, the plaintiffs claim that they did not discover that National had performed high-grading until after they filed their complaint in 1982.

The jury found and the trial court held that the defendants failed to act as a reasonably prudent operator when they failed to blend ore during the second run of production beginning in 1976. The court also held that the defendants acted in bad faith and failed to at as a reasonably product operator when they began high-grading ore in 1978. On appeal, the plaintiffs claim that the trial court correctly implied a duty of reasonable diligence and care upon the defendants, which the defendants breached when they failed to blend and failed to refrain from high-grading. The defendants claim that the express agreements between the parties supersede and foreclose the existence of any implied covenants.

1. *Construction of Contracts.*

In interpreting mining agreements, courts generally have applied the rules for interpreting contracts and leases. 4 *American Law of Mining* § 130.04, at 130-9 (2d ed.

1992). That is, courts will give effect to the intent of the parties, and when the terms of the agreement are clear and unambiguous, courts try to ascertain the intent of the parties from the ordinary meaning of the language in the agreement. *Id.* This has long been the rule in New Mexico: "The primary objective in construing a contract is to ascertain the intention of the parties." *Mobile Investors v. Spratte*, 93 N.M. 752, 753, 605 P.2d 1151, 1152 (1980). "The purpose, meaning and intent of the parties to a contract is to be deduced from the language employed by them; and where such language is not ambiguous, it is conclusive. The court's duty is confined to interpretation of the contract which the parties made for themselves and may not alter or make a new agreement for the parties." *Davies v. Boyd*, 73 N.M. 85, 87-88, 385 P.2d 950, 951 (1963).

We are impressed with a Texas Court's analysis of whether an implied covenant exists in the context of mining law, and we adopt it. The Texas Court of Civil Appeals has stated:

> In the outset it should be noted that when parties reduce their agreements to writing, the written instrument is presumed to embody their entire contract, and the court should not read into the instrument additional provisions unless this be necessary in order to effectuate the intention of the parties as disclosed by the contract as a whole. An implied covenant must rest entirely on the presumed intention of the parties as gathered from the terms as actually expressed in the written instrument itself, and it must appear that it was so clearly within the contemplation of the parties that they deemed it unnecessary to express it, and therefore omitted to do so, or it must appear that it is necessary to infer such a

> covenant in order to effectuate the full purpose of the contract as a whole as gathered from the written instrument. It is not enough to say that an implied covenant is necessary in order to make the contract fair, or that without such a covenant it would be improvident or unwise, or that the contract would operate unjustly. It must arise from the presumed intention of the parties as gathered from the instrument as a whole.

Kingsley v. Western Natural Gas Co., 393 S.W.2d 345, 350-51 (Tex.Civ.App.1965) (quoting *Danciger Oil & Refining Co. of Tex. v. Powell*, 137 Tex. 484, 154 S.W.2d 632 (1941)).

2. *Implied Covenants.*

Thus, implied covenants are not favored in law, especially when a written agreement between the parties is apparently complete. *Stern v. Dunlap Co.*, 228 F.2d 939, 942 (10th Cir.1955). The general rule is that an implied covenant cannot coexist with express covenants that specifically cover the same subject matter. *Kingsley*, 393 S.W.2d at 350.

When it is clear, however, from the relevant parts of the contract taken together and considered with the facts and circumstances surrounding the execution of the agreement, that the obligation in question was within the contemplation of the parties or was necessary to effect their intention, then such obligation may be implied and enforced. *Stern*, 228 F.2d at 942-43. But when the contract between the parties speaks to the obligation sought to be implied, courts will not write that implied obligation into the contract. *Kerr-McGee Corp. v. Bokum Corp.*, 453 F.2d 1067, 1073 (10th Cir.1972). Stated conversely, there may be

"an implied covenant on the part of the lessee (*in the absence of any expressed on the subject as in this lease*). . . . " *State ex rel. Shell Petroleum Corp. v. Worden*, 44 N.M. 400, 404, 103 P.2d 124, 126 (1940) (emphasis added).

3. *The provision granting defendants exclusive control.*

We believe that the express provisions in the contract according the defendants exclusive discretion and control in the mining operations left no room for the implied covenants that the trial court enforced against the defendants. The situation here is very similar to that discussed in an often-cited treatise.

> Instead of imposing duties upon the operator for the benefit of the owner of a nonoperating interest, the instrument creating the interest may contain a clause relieving the operator from certain obligations which might otherwise be alleged to exist. Such clauses take a variety of forms; typical is the following:
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> > "Development of, and operations on the premises, if any, and the extent and character thereof, as well as the preservation or forfeiture of the leasehold, shall be solely at the will of said (assignee) or its successors or assigns. . . . "

2 Howard R. Williams & Charles J. Meyers, *Oil and Gas Law* § 429, at 489-90 (1992). Here, the contract specified that "the nature and extent of all work done by Freeport on the Mining Lands and the time and manner of doing the same shall rest in the sole judgment and discretion of Freeport." The contract also stated that "the nature and

extent of all exploration, development and mining operations and the time and manner of performing the same shall be as Freeport in its sole judgment and discretion shall determine and Freeport shall have the right at all times to determine the quantity of ore to be mined and what ore is to be left unmined. . . . " In addition, the contract provided that National "may at any time and from time to time suspend mining operations or other operations for as long as it may determine whenever in its opinion economic conditions or other causes make it desirable so to do."

These express provisions supersede any implied obligation regarding operation of the mine and preclude the implication of any implied covenants advocated by the plaintiffs and enforced by the trial court. The implied covenants were not necessary to give effect to the intentions of the parties as reflected in the language of the contract. On the contrary, the implied covenants were inconsistent with the intentions of the parties as expressed in the written agreements. Given the specific language in the written agreements between the parties, it was error for the trial court to imply obligations that were inconsistent with the unambiguous language expressing the intention of the parties to extend the defendants absolute control over mining operations.

4. *The Lessor-Lessee Cases.*

Were it not for the express contractual provisions governing the relationship between the plaintiffs and the defendants and superseding any implied covenants, the

plaintiffs' argument would still fail. Much of the precedent that the plaintiffs cite in support of the implied covenants pertains to the relationship and the concomitant duties between a lessor and a lessee, not between the holder of an overriding royalty interest and a working interest (lessee), which was the relationship between the parties here. The trial court found that there was "no lessor-lessee relationship at any time" between the parties. Again, we find guidance from Williams & Meyers:

> The owner of an overriding royalty is not entitled to the benefit of the covenants of the base lease, express or implied, in the absence of an express provision in the instrument creating the overriding royalty. The benefits of such express and implied covenants of the lease touch and concern the lessor's estate and the burdens of such covenants touch and concern the lessee's estate. The assignment, either in whole or in part of the burdened estate, will not permit enforcement of the covenants which burden the assigned estate by a person other than the lessor or claimants through him of a portion or all of the benefitted estate.

2 *id.* § 420, at 356-57. Because the plaintiffs' cases pertain to the legal relationship between a lessor and lessee and not the rights of a lessee and a holder of an overriding royalty, the plaintiffs' cases are not persuasive.

There are occasions, however, when courts will imply covenants to protect the interests of an owner of an overriding royalty that is carved out of a working interest such as the case here. 2 *id.* § 420.1, at 356.1. The only instance in which courts seem to be in universal agreement is in implying a covenant against drainage in an oil

and gas lease. *See, e.g., Cook v. El Paso Natural Gas Co.*, 560 F.2d 978 (10th Cir.1977).

The plaintiffs rely heavily upon *Cook*, but we find the analogy from the covenant against drainage in an oil and gas lease to the mineral lease here untenable. The plaintiffs cite *Cook* for two propositions: that a lessee-operator has an implied duty to act in compliance with the reasonably prudent operator standard for the benefit of the nonoperator royalty holder; and that an express covenant does not necessarily negate the existence of an implied covenant. In *Cook*, however, the Tenth Circuit Court of Appeals held that an implied covenant obligating the lessee to act as a reasonably prudent operator did not apply. *Id.* at 984. Rather, the court held that an implied covenant existed obligating the operator to refrain from depleting gas on the owner's property by drainage from the operator's adjacent leasehold. Courts generally will uphold an implied covenant to protect against drainage because drainage is tantamount to conversion. *See id.* at 983. In addition, the *Cook* court did not go so far as to state categorically that an express covenant is always subject to implied obligations; rather, the court simply construed the express provision at issue in that case as ambiguous and found that it did not supersede an implied covenant against drainage. *Id.* at 986.

The plaintiffs also rely upon *Darr v. Eldridge*, 66 N.M. 260, 346 P.2d 1041 (1959), as upholding the trial court's finding of an implied covenant to exercise reasonable diligence. In *Darr*, this Court stated that "courts have developed the implied covenant 'to make diligent efforts to market the production in order that the lessor may realize on his royalty interest.' " *Id.* at 263, 346 P.2d at

1044 (citing *Libby v. De Baca*, 51 N.M. 95, 99, 179 P.2d 263, 265 (1947)). The plaintiffs' reliance again is misplaced; this is another lessor-lessee case. Nevertheless, the holding in *Darr* might support the plaintiffs' claim on the surrender breach (failing to market potash when National terminated production in 1968), but we have held that the six-year statute of limitations barred plaintiffs' claim on that issue. The plaintiffs were notified of the shut-down in 1968, and they could have brought an action supported by *Darr* and *Libby*, if any, then or six years thereafter, but that claim was time-barred by the time they filed their complaint in 1982.

5. *The Implied Covenant of Good Faith and Fair Dealing.*

In the absence of any covenants implied into the agreement between the parties, the owner of an overriding royalty interest is not without protection. Whether express or not, every contract in New Mexico imposes the duty of good faith and fair dealing upon the parties in the performance and enforcement of the contract. *Watson Truck & Supply Co. v. Males*, 111 N.M. 57, 60, 801 P.2d 639, 642 (1990). The breach of this covenant requires a showing of bad faith or that one party wrongfully and intentionally used the contract to the detriment of the other party. *Id.* The trial court found that the defendants acted in wanton disregard of the plaintiffs' interests by high-grading the ore in the Lea County mine. We cannot agree with the trial court that the defendants acted in bad faith by high-grading when the contract expressly gave them exclusive discretion in mining operations.

The covenant of good faith and fair dealing does not impose affirmative duties upon one party to protect another; instead, it proscribes action that in this case would have resulted in avoiding royalty payments. *See Tidelands Royalty "B" Corp. v. Gulf Oil Corp.*, 804 F.2d 1344, 1354 (5th Cir.1986). To show bad faith in this case, for example, the plaintiffs would have had to prove that the defendants would not have conducted a high-grading program in the absence of the overriding royalty interest, that by high-grading the defendants somehow sought to avoid making royalty payments.

Merely asserting that National failed to take action that might have been beneficial to the royalty holders does not show bad faith. Instead, the plaintiffs would have to prove that *but for* the pecuniary advantage of avoiding the royalty payments, the defendants would not have performed high-grading at the Lea County mine. *See id.* Adopting the plaintiffs' position (implying a duty to refrain from high-grading) would be the same as imposing a fiduciary duty upon the defendants, which we already have stated did not exist. The defendants were not obligated to act to their economic detriment for the benefit of the plaintiffs. *See Murdock v. Pure-Lively Energy 1981-A, Ltd.*, 108 N.M. 575, 579, 775 P.2d 1292, 1296 (1989) (covenants of good faith, unlike fiduciary duties, do not require exclusive operator to subordinate its interest to that of royalty holders). In fact, it could be said that high-grading was in furtherance of the royalty holders' interests. The aim of high-grading as the plaintiffs admitted is profits, albeit short-term profits. As long as the defendants were seeking profits, that was beneficial for the royalty holders and in furtherance of their interest. Any

resulting inconvenience in the retrieval of the remaining ore might constitute waste, but that would be actionable only by the lessor, not the holders of an overriding royalty interest.

6. *No Implied Covenants Existed.*

It was beyond question that the parties left the mining operation within the sole discretion of the defendants. National could exercise exclusive control, discretion, and judgment regarding all its operations and performance, and it could determine the quantity of ore mined and the quantity left unmined. In addition, National could elect to suspend operations "for as long as it may determine whenever in its opinion economic conditions or other causes make it desirable so to do." Implied covenants generally exist only in a lessor-lessee relationship, and covenants will not be implied when express contractual provisions govern, with the one exception of a covenant against drainage. Thus, the trial court erred as a matter of law in finding and enforcing implied covenants against the defendants that were inconsistent with the provisions of the written agreements. The trial court also erred when it held that the defendants' high-grading constituted bad faith when the contract allowed the defendants to conduct mining operations at their discretion. It would be incongruous to hold that the defendants acted in bad faith in acting in accordance with an express contractual provision.

V. *CONCLUSION*

As we have pored through the record in our consideration of the statute of limitations issue, we have tried to distinguish between what the plaintiffs knew or should have known and what the defendants did. We sympathize with the plaintiffs about the unfortunate events surrounding their agreement with the defendants, but the law requires a proper application of the doctrine of equitable estoppel for purposes of tolling statutes of limitations. Plaintiffs hoped, as did National, that the potash market would be favorable and that the Lea County mine would be highly profitable. While we might speculate now about what the defendants should or should not have done relative to their contractual duties, any breach of those duties was apparent to the plaintiffs long before 1976.

Although the circumstances turned out otherwise, as a matter of law the plaintiffs cannot second-guess business decisions made years ago in an attempt to recover damages unless they could prove that National concealed material facts and circumstances from them. The correspondence between the parties, however, shows a clear understanding on the part of both parties that they were dealing with an unpredictable market. The correspondence also demonstrates that the plaintiffs were aware of the defendants' alleged breaches, but failed to assert their legal rights until it was too late. The record indicates that the plaintiffs were or should have been aware of sufficient information upon which to allege a breach of contract claim as early as the 1960s.

Thus, the plaintiffs' claim of fraudulent concealment based upon alleged affirmative misrepresentations by the defendants fails because they were aware of those facts. Concerning the facts that the plaintiffs claim were not disclosed to them by the defendants, the defendants had no affirmative duty to disclose to the plaintiffs. Thus, there was no fraudulent concealment arising from the breach of a fiduciary duty either.

Pertaining to the blending and high-grading issues, the contracts between the parties were specific and unambiguous, leaving no room for the existence of implied covenants dealing with the same duties and obligations. The implies covenants imposed by the trial court were inconsistent with the express contractual provisions. National had the right to exercise exclusive control, discretion, and judgment regarding all mining operations, thus defeating the plaintiffs' claim as to blending. In addition, the defendants could determine the quantity of ore mined and the quantity left unmined, thus foreclosing the plaintiffs' argument regarding high-grading. It is not the function of the courts in this state to rewrite a contract by implying covenants between parties when an express written agreement exists. "There are some things the court cannot do and one is to do for the parties what they failed to do for themselves." *Kimberly, Inc. v. Hays*, 88 N.M. 140, 145, 537 P.2d 1402, 1407 (1975). Thus, the trial court incorrectly applied the law to the facts in this case by implying covenants against the defendants.

In sum, the trial court erred in holding that the breach of contract claims and the fraud claim were not barred by the applicable statutes of limitations. The trial

court abused its discretion in tolling the statutes of limitations. The record does not support the trial court's finding of fraudulent concealment nor the application of equitable estoppel to preclude the defendants from asserting the statute of limitations defenses. The trial court also erred as a matter of law in finding and enforcing implied covenants against the defendants. Accordingly, we vacate the jury's verdict and reverse the trial court's judgment that ratified the verdict.

IT IS SO ORDERED.

BACA and FRANCHINI, JJ., concur.

APPENDIX B

Order denying rehearing, New Mexico Supreme Court, No. 19,054 (September 23, 1993)

IN THE SUPREME COURT OF THE STATE OF NEW MEXICO

September 23, 1993

NO. 19,054

CONTINENTAL POTASH, INC., et al.,

Plaintiffs-Appellees and Cross-Appellants,

vs.

FREEPORT-McMORAN, INC., et al.,

Defendants-Appellants and Cross-Appellees.

This matter coming on for consideration by the Court upon appellees' motion for rehearing and amended motion for rehearing, and the Court having considered said motions and being sufficiently advised;

NOW, THEREFORE, IT IS ORDERED that the motions are DENIED.

ATTEST: A TRUE COPY

/s/ Kathleen Jo Gibson
Clerk of the Supreme Court
of the State of New Mexico

APPENDIX C

Excerpts from Plaintiffs-Appellees' Amended Motion for Rehearing, New Mexico Supreme Court, No. 19,054 (August 30, 1993)

IN THE SUPREME COURT
OF THE STATE OF NEW MEXICO

CONTINENTAL POTASH, CO., et al., Plaintiffs-Appellees, and Cross-Appellants,	)	
-vs-	)	No. 19,054
FREEPORT-McMORAN, INC. et al., Defendants-Appellants, and Cross-Appellees.	)	

APPEAL FROM THE DISTRICT COURT OF
SANTA FE COUNTY, JUDGE PETRA JIMENEZ MAES

PLAINTIFFS-APPELLEES' AMENDED MOTION FOR REHEARING

(Filed Aug. 30, 1993)

AMENDED MOTION FOR REHEARING

Plaintiffs-Appellees move for rehearing en banc of the Opinion of August 10, 1993, pursuant to NMSA 1978, SCRA 12-404(A) and *Boudar v. E.G. & G., Inc.*, 106 N.M.

279, 742 P.2d 491 (1987) (rehearing granted after denial of first motion for rehearing).

1. The Opinion violates the Supremacy Clause, Art. VI, cl. 2, of the United States Constitution, in that it construes a contract assigning mineral rights on the public lands in such a way as to undermine federal policy and regulations barring waste and requiring ultimate maximum recovery of mineral resources under the Mineral Leasing Act of 1920, 30 U.S. 181 *et. seq.*

> Although federal law does not govern all questions of contract interpretation involving leases issued under the Mineral Leasing Act of 1920 [citation omitted], it applies to questions with significant implications for federal policy and which require uniform resolution throughout the federal system.

Lowey v. Watt, 684 F.2d 957, 965 (D.C.Cir. 1982); *and see, Coyer v. Watt,* 720 F.2d 626 (10th Cir. 1983); *cf., Boesche v. Udall,* 373 U.S. 472 (1963) and *Harvey v. Wall,* 384 F.2d 883 (10th Cir. 1967) a case arising in New Mexico. The Opinion further violates federal common law of mining which is consistent with the federal regulations. *Brewster v. Lanyon Zinc,* 140 Fed. 801 (8th Cir. 1905).

The Opinion concedes the contract of assignment incorporates federal anti-waste regulations (Op. at 5). (The regulations are set forth in TR 197 *et. seq.*) It concedes that the jury awarded damages to Plaintiffs based on Freeport's waste (Op. at 9, fn. 6). It now concedes "we view the district court's findings of fact most favorably for the appellee, indulging all reasonable inferences in its favor." (Op. at 11) But it holds that the damage caused by

Freeport's waste was actionable only by the federal government because, as a matter of (unspecified) law, whenever an operator engages in highgrading or is otherwise "seeking profits" then it is necessarily acting in the interests of the holders of an overriding royalty interest regardless of the waste, which becomes inactionable. (Op. at 29). That holding has "significant implication for federal policy," *Lowey, supra* at 965, because it effectively bestows on Defendants a license to waste.

Without citation the Opinion declares:

> In fact, it could be said that high-grading was in furtherance of the royalty holders' interests. The aim of high-grading as the plaintiffs admit is profits, albeit short term profits. As long as the defendants were seeking profits, that was beneficial for the royalty holders and in furtherance of their interests. Any resulting inconvenience in the retrieval of the remaining ore might constitute waste, but that would be actionable only by the lessor (the federal government), not the holders of an overriding royalty interest.

Op. at 29.

The premise for this conclusion is that the interests of defendants with regard to highgrading were parallel to those of the Plaintiffs (Op. pp. 28-29). The record does not support this premise. The interests of the operator and the royalty holder in a net profits royalty arrangement are not always parallel and were not parallel here. (Appendix B) Freeport's interests conflicted with Plaintiff's; see *infra*, p. 6. Even by the reasoning of the Opinion highgrading could only benefit Plaintiffs if Freeport had an intention of overcoming the loss carry forward. But, as Nelson

observed, Freeport's potash venture was "not market driven" (Depos of Nelson, p. 260). Moreover, the inference of "He should live so long" (Ex. 350) is that Freeport had no intention of showing profit in McGreevy's lifetime. *See, also,* Trial exhibits 164, 174, 174A; 322, p. 15; 370.

The Opinion defies common sense in holding that waste is a benefit to net profits royalty holders with reversionary rights. Not even the Defendants took the position at trial that they had the right under the contract to commit waste. (Appendix B, Tr. 1674, 1677) Never before has a court to our knowledge held as a matter of law that highgrading is beneficial. *See* Black's Law Dictionary, Fifth Ed., "Highgrading. The practice, in mining vernacular, of stealing ore. *People v. Siderius,* 29 Cal.App.2d 361, 84 P.2d 545, 547." Highgrading is not prudent because it sacrifices ultimate maximum recovery for short term results. *Dawn Mining Co. v. Watt,* 543 F.Supp. 841 (D.C.D.C. 1982), aff'd 704 F.2d 1293. In this case highgrading destroyed the commercial recoverability of one tenth of all domestic potash reserves discovered by 1982. Denying a private contract remedy here flies in the face of national policy. The Opinion "stands as an obstacle to the accomplishment of the full purposes and objectives of Congress." *Ramah Navajo School Board v. Bureau of Revenue of New Mexico,* 458 U.S. 832, at 845 (1982) citing *Hines v. Davidowitz,* 312 U.S. 52, 67 (1941).

2. The Opinion violates due process and equal protection of law guaranteed plaintiffs by the 5th and 14th amendments to the United States Constitution, in that it abandons the normal standard of judicial review, normal

substantive law, and normal derivation of facts from evidence in order to achieve a favored result. *Rask v. Board of Bar Examiners,* 75 N.M. 617, 624-625, 409 P.2d 256 (1966) (deviation from established rule or practice violates due process); *Youngberg v. Romeo,* 457 U.S. 307 (1982) (arbitrary and capricious conduct when decisions are made contrary to professional standards); *Motor Vehicle Mfger's Ass'n v. State Farm Mutual,* 463 U.S. 29 (1983) (arbitrary and capricious behavior to offer an explanation for decision which runs counter to evidence or fails to consider an important aspect of the problem); *New York Times v. Sullivan,* 376 U.S. 254, 285, fn 26 (1964) (rule of law applied by Alabama courts was constitutionally deficient for failure to provide the safeguards for freedom of speech and of the press that are required by the First and Fourteenth Amendments; Supreme Court would review the evidence to make certain that those principles have been constitutionally applied).

A. The Opinion abandons the normal standard of judicial review by ignoring findings and creating its own facts (e.g., highgrading is good and Plaintiffs had access to potash prices). *Smith v. McKee,* ___ N.M. ___, Slip Opinion, No. 20,387, August 18, 1993, page 5 (recognizing that appellate court will not determine facts on appeal).

A main pillar of the holding as to fraudulent concealment is the assertion that McGreevy was on the board of a company in the potash market with access to market information.

> The plaintiffs stated that no one outside the potash industry could learn the price of potash. Yet, McGreevy sat on the Board of directors of a company that was also in the potash market.

> Thus, if the plaintiffs were not aware of material facts, McGreevy and the others could have discovered the material facts through exercise of due diligence.

Op. p. 17. This unsupported "fact" is the sole buttress for the central conclusion there was no fraudulent concealment regarding marketing breaches. However, this "fact" defies all record testimony, attached hereto as Appendix "A"[1] and D and the trial court's findings nos. 20, 39, 40, 41, 46, 48, 49, 50, 56, 57, 69. The "fact" is created out of whole cloth.

McGreevy was not on the board of a company in the potash market and had no access to potash market information other than through Defendants. When his early inquiries and threats of litigation over the CF contract were met with National's explanations, particularly the lulling Wells letter of May 5, 1962 (Trial Exhibit 139) describing the CF contract and the potash price structure he was unable to prove differently and was not required to disbelieve his partner and sue. *Gaston v. Hartzell*, 89 N.M. 217, 219, 549 P.2d 632 (Ct.App. 1976); *Ferrell v. Ferrell*, 719 P.2d 1, 5 (Kan. 1986); *Bellingham Securities Syndicate v. Bellingham Coal Mines*, 125 P.2d 668, 677 (Wash. 1942).

Of course the Wells letter with its omission of the interlocking directorate with CF and its bland assurance

---

[1] Appendix A incorporating Tabs "A through I" is attached to the motion for rehearing filed August 23, 1993; but see also TR 206 (attached as Appendix D) in which Freeport admits, "We do not know of any reliable or accurate source of information concerning potash prices on the open market."

of uniform market prices was false. With no sales force, not even Freeport could access the market price of potash and relied on its customer to tell it. Unknown to plaintiffs, Freeport's potash deal with CF was never market driven, it was a sales pitch for other Freeport products. See Findings 48, 49, 50, 51 and evidence supporting them, Appendix A to motion for rehearing and Appendix A to Answer Brief.

B. The Opinion cavalierly abandons substantive law of contract interpretation by failing to give effect to the express intentions of the parties to bind the assignee, Freeport, to its federal lease and its controlling regulations, *C.R. Anthony, Inc. v. Loretto Mall Partners*, 112 N.M. 504, 817 P.2d 238 (1991) and, in this case, to acknowledge and conform its interpretation to governing federal policies, law, and regulations. *Lowey v. Watt, supra.*

Additionally, in reaching its construction of the contract, the Opinion creates a further fact not supported by the evidence and contrary to the findings below (nos. 19, 43, 58, 59 and 60), to wit, that Defendants used due diligence in good faith by highgrading the mine. In fact, there was substantial evidence to the contrary. *See* Appendix A to Answer Brief and Appendix A to first motion for rehearing.

3. The Opinion also violates due process by failing to recognize the verdict of the jury and findings of the trial court of other breaches and frauds *within* the limitations period which are sufficient to save the verdict. See Findings 53, 61, 62, 63, 64, 65, 72 and 79. Apart from highgrading the jury and trial court found significant

accounting breaches and breaches of the marketing duty occurring within six years of the filing of this action.

4. The Opinion further violates due process in failing to address the finding of continuing fraud, Findings 71 and 78, which prevented plaintiffs from suing earlier and which tolled the limitations period. *Bellingham, supra.*

5. Although current construction of the Contracts Clause, Art. I, sec. 10, cl. 1, of the United States Constitution does not recognize a violation of the impairments clause by judicial action the doctrine is mainly a matter of dicta, it does not conform to the early interpretation and should be changed, as the dichotomy is not logical. The Opinion violates the Contracts Clause and should be reversed. The impairment here constitutes a form of judicial legislation barred by the clause.

6. The Opinion violates Art. II, sec. 12 of the Constitution of New Mexico which holds inviolate trial by jury. The arbitrary refinding of facts found by the jury violates this clause and the Due Process Clause of the 5th and 14th Amendments to the United States Constitution. *Cf.*, 7th Amendment to the United States Constitution.

CONCLUSION

The Opinion strips away some gratuitous anomalies of the Decision but it still bears signs of its unpublished genesis. If allowed to stand it will blot New Mexico jurisprudence. Plaintiffs have been denied valuable rights flowing from the Mineral Leasing Act of 1920, *supra,* preserved in their contract of assignment.

Plaintiffs pray for withdrawal of this Opinion, reinstatement of the jury verdict, vacation of the mandate, rehearing en banc, and substitution for any justice who may recuse himself. In the alternative, the case should be remanded for assessment of damages for breaches and frauds occurring within the limitations periods. Plaintiffs-Appellees pray also for such other and further relief as this Court deems just.

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APPENDIX C – Highgrading, pp. 1258-1259

Testimony of John Burleson

* * *

Q So waste by your definition has nothing to do with bad intentions – I will stop there.

A In the year of 1978 of which I am very familiar because I was there and I had researched all of the documents that we received from National and Freeport, the waste that year was intentional. The high-grading was intentional. The movements, so many times at such a high price, that was intentional.

It was a frantic reckless operation on the part of National during that year. Pressure was coming from New York, pressure to made money, make money, we are losing money, high-grade.

We have the documents offered into evidence. High-grade even if it sacrifices the ore reserves, do this, do that. That was a frantic and reckless year as the documents show us.

Q To get off of this, what you are saying is, your criticism from your own eyeballs of high-grading has to

do with the pillars that we left there without pulling them; is that correct?

A Partially.

Q Your criticism of high-grading independent of that is based on documents that you have read that we provided in the discovery phase of this lawsuit where we used the phrase, high-grading, several times?

A Yes.

Q If it turns out that the company was using that phrase in the sense of, look, as you have said, we are not making any money, we are mining stuff here that is not economic, it is not good ore, go find the good ore. If that is what we meant by high-grading, would you be critical of that?

A Yes, because in that same sentence, do it no matter what the cost to the ore body, do it even if it means that we lose reserves. You have read those sentences. It was high-grading and that is wrong.

APPENDIX D

Excerpts from Plaintiffs-Appellees' Motion for Rehearing, New Mexico Supreme Court, No. 19,054 (August 23, 1993)

IN THE SUPREME COURT
OF THE STATE OF NEW MEXICO

CONTINENTAL POTASH, CO., et al., Plaintiffs-Appellees, and Cross-Appellants, -vs- FREEPORT-McMORAN, INC. et al., Defendants-Appellants, and Cross-Appellees.	No. 19,054

APPEAL FROM THE DISTRICT COURT OF
SANTA FE COUNTY, JUDGE PETRA JIMENEZ MAES

PLAINTIFFS-APPELLEES' MOTION FOR REHEARING

(Filed Aug. 23, 1993)

MOTION FOR REHEARING

Plaintiffs-Appellees move for rehearing en banc of the Opinion of August 10, 1993, pursuant to NMSA 1978, SCRA 12-404(A) and *Boudar v. E.G. & G., Inc.*, 106 N.M.

279, 742 P.2d 491 (1987) (rehearing granted after denial of first motion for rehearing).

1. The Opinion violates the Supremacy Clause, Art. VI, cl. 2, of the United States Constitution, in that it applies state law construction to a contract assigning mining rights under the Mineral Leasing Act of 1920, 30 U.S.C. 181, *et seq.*, so as to undermine federal policy and regulations barring waste and requiring ultimate maximum recovery of mineral resources in the public lands.

> Although federal law does not govern all questions of contract interpretation involving leases issued under the Mineral Leasing Act of 1920 [citation omitted], it applies to questions with significant implications for federal policy and which require uniform resolution throughout the federal system.

Lowey v. Watt, 684 F.2d 957, 965 (D.C.Cir. 1982); *and see, Coyer v. Watt*, 720 F.2d 626 (10th Cir. 1983); *cf., Boesche v. Udall*, 373 U.S. 472 (1963) and *Harvey v. Wall*, 384 F.2d 883 (10th Cir.-N.M. 1967). The Opinion further violates federal common law of mining which is consistent with the federal regulations. *Brewster v. Lanyon Zinc*, 140 Fed. 801 (C.C.A. 8th 1905).

The Opinion concedes the contract of assignment incorporates federal anti-waste regulations (Op. at 5). It concedes that the jury awarded damages to Plaintiffs based on Freeport's waste (Op. at 9). It now concedes "we view the district court's findings of fact most favorably for the appellee, indulging all reasonable inferences in its favor." (Op. at 11) But it holds that the damage caused by

Freeport's waste was actionable only by the federal government because, as a matter of (unspecified) law, whenever an operator engages in highgrading or is otherwise "seeking profits" then it is necessarily acting in the interests of the holders of an overriding royalty interest regardless of the waste. (Op. at 29). That holding has "significant implication for federal policy," *Lowey, supra* at 965, and is therefore preempted. The jury found highgrading damaged Plaintiffs. Adequate evidence and findings (nos. 58, 59 and 60) support the fact highgrading was not a benefit. The waste took place within the limitations period under New Mexico law. (Op. at 22) The jury verdict should be reinstated.

2. The Opinion violates due process and equal protection of law guaranteed plaintiffs by the 5th and 14th amendments to the United States Constitution, in that it abandons the normal standard of judicial review, normal substantive law, and normal derivation of facts from evidence in order to achieve a favored result. *Rask v. Board of Bar Examiners,* 75 N.M. 617, 624-625, 409 P.2d 256 (1966) (deviation from established rule or practice violates due process); *Youngberg v. Romeo,* 457 U.S. 307 (1982) (arbitrary and capricious conduct when decisions are made contrary to professional standards); *Motor Vehicle Mfger's Ass'n v. State Farm Mutual,* 463 U.S. 29 (1983) (arbitrary and capricious behavior to offer an explanation for decision which runs counter to

* * *

Testimony of Menefee Blackwell

Q Let me drop back a little bit; Mr. Milton McGreevy was a close friend. How would you describe him as a businessman?

A He was a stockbroker first, he was an experienced investor.

Q Did you know if he had any experience in the mining industry:

A He had none.

Q Did he have any experience in the potash field?

A I am sure he had none.

Q Did you know if he ever visited the mine?

A Not to my knowledge, and I feel sure that he did not. If he had, I probably would have gone with him.

Q Did you know Walter Cross?

A Yes, he has been dead for many years now.

Q Do you know if he was involved in the mining business at all?

A Well, Kansas City Testing Labs which now is called Cross Labs, had not engaged in mining itself. They had some peripheral association with Sulphur mining, but nothing to do with potash.

Q To your knowledge, was that the extent of Mr. Cross' involvement in mining?

A As far as I know.

* * *

Q Spencer Chemical was in the fertilizer business; is that what you said?

A Yes, among other things.

Q To be on the board of a fertilizer company, that would require an intense working knowledge of the pricing mechanisms in the industry; is that a fair statement?

A No. I disagree entirely. If you are getting at, did he know the price of potash, he could not find that out.

Q Why not?

A I don't know. He reported to me that he could not ever find out.

* * *

APPENDIX E

Excerpts from Plaintiffs-Appellees' Reply Brief in Support of Rehearing, New Mexico Supreme Court, No. 19,054 (July 6, 1993)

IN THE SUPREME COURT
OF THE STATE OF NEW MEXICO

CONTINENTAL POTASH, CO., et al., Plaintiffs-Appellees, and Cross-Appellants, -vs- FREEPORT-McMORAN, INC. et al., Defendants-Appellants, and Cross-Appellees.	No. 19,054

APPEAL FROM THE DISTRICT COURT OF
SANTA FE COUNTY, JUDGE PETRA JIMENEZ MAES

PLAINTIFFS-APPELLEES' REPLY BRIEF IN SUPPORT OF REHEARING

(Filed July 6, 1993)

I. THE CONTRACT DOES NOT GIVE FREEPORT UNFETTERED CONTROL.

A. The "subject to" language cannot be read out of the Contract.

Freeport writes the "subject to" phrase out of the contract by claiming that they are not words "of

contract", citing *S.T. McKnight Co. v. Central Hanover Bank & Trust Co.*, 120 F.2d 310 (8th Cir. 1941). That case involved an attempt by an owner/lessor to impose contractual duties on an assignee who had long since abandoned the property. The court held that the "assignee was bound to the lessor by privity of estate only and obligated to perform the covenants only while he was in possession of the leased premises." Id. at 320. Since there was no privity of contract and the assignee was no longer in possession the lessor's claim failed. Because the instant case does not involve duties owed by an assignee to a lessor, "privity of estate," or an absence of privity of contract, and because NPC was in possession, the *McKnight* case cannot support Freeport's position or the Decision of the Court.

The agreement of NPC and Freeport to abide by the federal leases and regulations was a contractual promise made directly to Continental, et. al., as assignors. The question for this Court is what did the parties intend by the "subject to" language. The language is a part of the contract and must therefore be construed to have contractual significance. The only logical conclusion is that these words served as limitations and restrictions on Freeport/NPC's control and discretion.

B. The 1948 Agreement, Paragraph 7e, controls and was not superseded.

The 1948 agreement, Paragraph 7e, settles the question of what duties of diligence Freeport owed Continental. Now, Freeport argues that the 1948 agreement was superseded by the 1951 agreement. The 1951 Agreement

(Ex. 3) did not alter the rights and duties of the 1948 agreement; it did not involve Continental. And nothing in the later contractual documents abrogates Paragraph 7e of the 1948 Agreement. (Ex. 1) Moreover, Freeport has admitted the 1948 agreement is part of the contract. (RP 2, 79, 385, 1124, 1598, 1792, and 1824.) These citations contain Freeport admissions that the 1948 Agreement was part of the contract in the form of answers to the first and amended complaints, stipulations in the pretrial order, Defendants' proposed voir dire orientation statement, and proposed jury instruction on the contract claim. Moreover, Findings 15 and 23 (that the 1948 Agreement was still in effect) were not objected to.

C. The Parties Have Expressly Adopted The Substance Of The Implied Covenants.

Freeport cites *Carma Developers v. Marathon Dev. Cal.,Inc.*, 826 P.2d 710 (Cal. 1992) a bizarre real estate decision in which the entire California Supreme Court recused itself. The rule in mining contracts is different, as shown by the extensive authority cited in the Brief in Support of this motion at 6 fn. 1. *And, see, e.g., Piney Woods Country Life School v. Shell Oil Co.*, 726 F.2d 2251 (5th Cir. 1984); *c.f., Greer v. Salmon*, 82 N.M. 245, 479 P.2d 294 (1970) (mineral lease is to be construed most strongly against lessee.) This rule evolved because of the importance of the policy announced in the seminal decision of *Brewster v. Lanyon Zinc*, 140 Fed. 801 (CCA 8 1905): when a large mining operator obtains mining rights from a small operator or landowner for a royalty it must mine for mutual benefit and not solely for its own profit. This

is the law of New Mexico. *Darr v. Eldridge*, 66 N.M. 260, 346 P.2d 1041 (1959).

Since the implied covenants harmonize with the 1948 agreement and the 1951 "subject to" language, they were properly charged to the jury. Freeport acknowledged the substance of this point in requested jury instructions (RP 1826, 1828, 1829, 1836, 1842, and 1841) at least insofar as prudent operation considering both the interests of Continental and National, marketing at prevailing price, and duties of good faith are concerned.

Finally, Freeport cites the Decision's comment that highgrading might be waste but is actionable only by the federal government. This comment fails to consider the limited resources of the Federal Government to enforce even blatant violations of federal regulations on government mining properties (Burleson testimony, TR 1207-1219). Further it fails to recognize Plaintiffs' reversionary interests or the fact that the contracts of assignment had to be approved by the Federal Government. (See, e.g., Ex. 2, which attaches an approval by the Secretary of the Interior's designee.)

* * *

FOR THESE REASONS, Plaintiffs-Appellees respectfully pray for the relief asked in their amended motion

for rehearing en banc and for such additional and further relief as the Court deems just.

Respectfully submitted:

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By: /s/ Michael P. Gross
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and

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APPENDIX F

Plaintiffs-Appellees' Amended Motion for Rehearing En Banc, New Mexico Supreme Court, No. 19,054 (May 24, 1993)

IN THE SUPREME COURT
OF THE STATE OF NEW MEXICO

CONTINENTAL POTASH, CO., et al., Plaintiffs-Appellees, and Cross-Appellants, -vs- FREEPORT-McMORAN, INC. et al., Defendants-Appellants, and Cross-Appellees.	No. 19,054

APPEAL FROM THE DISTRICT COURT OF
SANTA FE COUNTY, JUDGE PETRA JIMENEZ MAES

PLAINTIFFS-APPELLEES' AMENDED MOTION FOR REHEARING EN BANC

(Filed May 24, 1993)

In order to more particularly specify the bases for this petition, Plaintiffs-Appellees respectfully amend their motion for rehearing en banc filed May 5, 1993.

There has been no response to the petition to date and Appellees rely on their briefs of record in support of this petition:

By and through their attorneys and pursuant to SCRA 12-404 of the Rules of Appellate Procedure, Plaintiffs-Appellees respectfully move for rehearing by the full Court of the decision dated April 22, 1993, on the grounds that:

A. The decision disregards controlling precedent; applies an incorrect standard of review; changes fundamental mining and commercial law in New Mexico without publication in violation of SCRA 12-405; violates the rule governing when decisions must be issued under SCRA 12-406; misreads, misstates, and ignores fundamental facts of record; and fails to dispose of all the issues.

B. Plaintiffs-Appellees have been deprived of a benefit conferred by the Mineral Leasing Act of 1920, 30 U.S.C. §§181 et seq., especially §§211-214, by a surprise decision of the Mexico Supreme Court employing a legally incorrect standard of review which fails to apply federal and state mining and natural resource laws, policies and regulations (Ex. 476) (30 C.F.R. Part 231, esp. 231.12, 231.13, 231.14, 231.24, 231.27 [1938 and 1949 editions]) with profound national implications.

C. The manner of this decision, to-wit, by creation of facts not of record, disregard of evidence, adjustment of appellate law, and disregard of controlling precedent, coupled with non-publication (hence changing the law for these parties alone), violates Appellees' rights to Due Process and Equal Protection of the laws as provided to

them by the Fifth and Fourteenth Amendments to the United States Constitution by depriving them of fundamental fairness, equal treatment, and accepted standards of contractual, judicial and commercial law.

Plaintiffs additionally move for oral argument on all aspects of this motion. Plaintiffs additionally move that due to the far reaching issues presented, that the Court sit *en banc*, restore the jury verdict, and publish its ruling as an opinion.

Plaintiffs further move that if one of the justices should recuse himself from participation in the instant motion for rehearing considering this motion, another Judge be designated from the Court of Appeals to sit for purposes of reviewing the matters raised by the instant motion. In this manner, this motion will receive full review. A full panel is necessary to consider this motion in light of the importance of the issues presented by the instant motion. Plaintiffs finally move that the Court of Appeals Judge so designated sit as part of the *en banc* panel for purposes of reviewing the issues raised in this appeal and issuing an opinion.

Because of the nature of this motion, the consent of opposing counsel has not been sought.

WHEREFORE, Plaintiffs-Appellees respectfully request that the Court designate a Judge from the Court of Appeals, if necessary, to sit on the Supreme Court for purposes of considering all matters raised in this motion, that the Court grant oral argument on this motion, that the Court grant rehearing and grant oral argument on such areas as the Court directs, that the Court restore the

jury verdict and publish its ruling as an *en banc* opinion, and grant such other and further relief as is deemed just.

Respectfully submitted:

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On Brief:
C. Bryant Rogers

Of Counsel:
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Counsel for Plaintiffs-Appellees

APPENDIX G

Excerpt from 1948 Agreement, Trial Exhibit 1, paragraph 7e, *Continental Potash, Inc., et al. v. Freeport-McMoran, Inc., et al.*, District Court of New Mexico, County of Santa Fe, No. SF 82-218(C)

e) Freeport shall agree to use reasonable diligence and care in exploiting the deposit and all parties agree to use reasonable diligence and care to keep the leases in good standing and to comply with all Federal and State regulations pertaining to potash.

* * *

Freeport Sulphur Company
By s/ W.T. Lundy
Vice President

Accepted this 21st day
of July, 1948

Continental Potash Company

By s/ Walter M. Cross. Jr.
J. G. Hawthorne
Anne H. Cross
Walter M. Cross, Jr.

APPENDIX H

Excerpt from 1951 Agreement, Trial Exhibit 3, paragraph 8, *Continental Potash, Inc., et al. v. Freeport-McMoran, Inc., et al.*, District Court of New Mexico, County of Santa Fe, No. SF 82-218(C)

8. FREEPORT covenants and agrees that if FREEPORT exercises its option to acquire the Mining Rights as provided in Paragraph 5, FREEPORT will use its best efforts to secure at the proper time the granting of leases on any Permits as to which leases have not already been granted, and that thereafter it will maintain such leases in force and effect and develop and operate the Mining Lands in accordance with the provisions of the leases, paying all taxes and rentals becoming due thereunder, always subject, however, to the provisions of Paragraphs 11, 12 and 13. Subject to the requirements of the leases, the nature and extent of all exploration, development and mining operations and the time and manner of performing the same shall be as FREEPORT in its sole judgment and discretion shall determine, and FREEPORT shall have the right at all times to determine the quantity or ore to be mined and what ore is to be left unmined, and may at any time or from time to time suspend mining operation or other operations for as long as it may determined whenever in its opinion economic conditions or other causes make it desirable so to do.

APPENDIX I

Excerpt from Potassium Lease, May 6, 1953, Trial Exhibit 6, paragraph k, *Continental Potash, Inc., et al. v. Freeport-McMoran, Inc., et al.*, District Court of New Mexico, County of Santa Fe, No. SF 82-218(C)

(k) *Diligence. Prevention of Waste. Health and Safety of Workmen.* To develop and produce in commercial quantities, with reasonable diligence, skill and care in the operation of the property, the potassium and other mineral deposits susceptible of such production in the lands covered hereby; to carry out, at the expense of the leases, all reasonable orders of the Secretary, or his authorized representatives (Regional Mining Supervisors, Geological Survey), issued in pursuance of the operating regulations; to carry on all mining, reducing, refining, and other operations in accordance with approved methods and practice and in conformity with the operating regulations to the satisfaction of said representative; to take all reasonable precaution to prevent damage to mineral deposits, injury to life, health, or property, or economic waste; to restrict the workday to not exceeding eight hours in any one day for underground workers, except in cases of emergency; to employ no boy under the age of 16 and no girl or woman, without regard to age, in any mine below the surface; to observe all laws relative to the health and safety to workmen and employees; and to provide access at all times to mining and related productive operations for examination and inspection by authorized representatives of the lessor.

APPENDIX J

Excerpts from Jury Instructions, District Court of New Mexico, *Continental Potash, Inc., et al. v. Freeport-McMoran, Inc., et al.*, County of Santa Fe, No. SF 82-218(C) (July 7, 1989)

FIRST JUDICIAL DISTRICT)
COURT COUNTY OF SANTA FE)
STATE OF NEW MEXICO)
)
No. SF 82-218(C))
)
CONTINENTAL POTASH, INC., et al.,)
)
Plaintiffs,)
)
vs.)
)
FREEPORT-McMORAN, INC., et al.,)
)
Defendants.)
)

COURT'S INSTRUCTIONS

/s/ Petra J. Maes
DISTRICT JUDGE

INSTRUCTION NO. 3

This is a civil case in which the Plaintiffs claim to be entitled to money damages from the Defendants for breach of contract and fraud, by improper actions in the mining of leaseholds assigned to them by the Plaintiffs.

The parties admit the making of a contract under which the Plaintiffs assigned their federal potassium mining permits and leases in Lea County, New Mexico to the

Defendants to mine in exchange for a royalty of 8% of net divisible profits derived from production of potash from the leased lands.

The contract consists of the 1948 letter agreement, the 1949 First KCTL Agreement, the 1951 Second KCTL Agreement, the 1953 Mary Borders Byrte Agreement, and the 1956 Pooling Agreement, together with the underlying federal lease terms which those agreements incorporate, and together with the federal mining regulations which those lease terms incorporate.

The contract further consists of implied terms derived from custom and usage of the mining industry.

INSTRUCTION NO. 12

There was in force at the time of the formation of the contract between plaintiffs and defendants a certain federal regulation which provided that:

> 30 C.F.R. 231.13 OPERATIONS SHALL BE CONDUCTED IN A MANNER TO YIELD ULTIMATE MAXIMUM RECOVERY: INFORMATION RECORDED AND COPY FURNISHED DISTRICT MINING SUPERVISOR. Mining operations shall be conducted in a manner to yield the ultimate maximum recovery of the mineral deposits. All shafts, main exits and passageways, as well as overlying beds or mineral deposits that at a future date may be of economic importance shall be protected by adequate pillars in the deposit being worked. Information obtained regarding the mineral deposit being worked and other mineral deposits on the leased lands shall be fully

recorded and a copy of the record furnished to the district mining supervisor.

APPENDIX K

Excerpts from Pre-Trial Order, *Continental Potash, Inc., et al. v. Freeport-McMoran, Inc., et al.*, District Court of New Mexico, County of Santa Fe, No. SF 82-218(C) (May 11, 1989)

FIRST JUDICIAL DISTRICT COURT
COUNTY OF SANTA FE
STATE OF NEW MEXICO

No. SF 82-218(C)

CONTINENTAL POTASH, INC.,
et al.,

Plaintiffs,

vs.

FREEPORT-McMORAN, INC.,
et al.,

Defendants.

* * *

i. Whether Defendants breached their federal leases and thereby their agreements with Plaintiffs by committing economic waste and by not operating with due skill and care.

* * *

j. Whether Defendants breached their federal leases and thereby their agreements with Plaintiffs by committing economic waste.

* * *

APPENDIX L

Special Interrogatories and Verdict, *Continental Potash, Inc., et al. v. Freeport-McMoran, Inc., et al.*, District Court of New Mexico, County of Santa Fe, No. SF 82-218(C) (November 22, 1989)

FIRST JUDICIAL DISTRICT COURT
COUNTY OF SANTA FE
STATE OF NEW MEXICO

No. SF 82-218(C)

CONTINENTAL POTASH, INC.,
et al.,

Plaintiffs,

vs.

FREEPORT-McMORAN, INC.,
et al.,

Defendants.

SPECIAL INTERROGATORIES
AND VERDICT

(July 7, 1989)

CLAIM I

Do you find that Defendants breached their implied duty to act as a reasonably prudent operator by:

1. Failing to blend Lea County ore with Eddy County ore or other higher grade ore during the years 1968 and after?

a) Yes X No _

If your answer is "yes", did this result in damage to Plaintiffs?

b) Yes _ No X

2. High grading the Lea County Mine?

a) Yes X No _

If your answer is "yes", did this result in damage to Plaintiffs?

b) Yes X No _

3. Failing to keep National Potash Company adequately capitalized?

a) Yes _ No X

If your answer is "yes", did this result in damage to Plaintiffs?

b) Yes _ No _

4. Failing to keep the facilities and equipment necessary to prudently mine Lea County ore adequately maintained and repaired?

a) Yes _ No X

If your answer is "yes", did this result in damage to Plaintiffs?

b) Yes _ No _

5. Failing to sell the product from the Lea County Mine at the prevailing market price, which is the highest and best price obtainable by the exercise of reasonable effort?

a) Yes X No _

If your answer is "yes", did this result in damage to Plaintiffs?

b) Yes X No _

6. Failing to account with fidelity and charging Plaintiffs' royalty account with improper charges?

a) Yes X No _

If your answer is "yes", did this result in damage to Plaintiffs?

b) Yes X No _

IN THE ALTERNATIVE

Do you find that Defendants have breached their implied duty to act as a reasonably prudent operator by:

Keeping the leases and not surrendering them back to Plaintiffs when the Defendants knew or should have known that this would produce no economic benefit for Plaintiffs?

a) Yes X No _

If your answer is "yes", did this result in damages to Plaintiffs?

b) Yes X No _

INSTRUCTIONS

1. If you answered "yes" to both the "a" and "b" portions of any of the above questions, then you should proceed in awarding damages to Plaintiffs. If you did not so answer, please continue on to Claim II.

Please note that Plaintiffs have alternative claims under Claim I which are designed to avoid any chance of

a double recovery for breach of contract. Plaintiffs are entitled to recover damages based upon that alternative claim under Claim I which results in the highest damages, if the amounts are different.

DAMAGE AWARD

Plaintiffs are entitled to damages as against Defendants in the amount of

$ 1, 816, 690. 23

CLAIM II

Did the Defendants commit fraud upon the Plaintiffs?

a) Yes X No _

If your answer is "yes", did this result in more than nominal damages to Plaintiffs?

a) Yes X No _

Additionally, if your answer to the last question was "yes", do the damages for fraud coincide with the damages, if any, awarded under Claim I?

a) Yes X No _

If your answer to the last question is "no", please state the additional amount of damages to Plaintiffs for fraud:

$ 0 .

INSTRUCTIONS

If you did not award damages under either Claim I or Claim II then you should stop and have the Foreman sign this form. If you have awarded damages under either Claim I or Claim II then you should proceed to Claim III.

CLAIM III

Do you find that punitive damages should be assessed against the Defendants?

a) Yes X No _

If your answer is "yes", please state the amount:

$ 3, 000, 000

/s/ Ronald E. Hassett
FOREMAN

APPENDIX M

Findings of Fact and Conclusions of Law, *Continental Potash, Inc., et al. v. Freeport-McMoran, Inc., et al.*, District Court of New Mexico, County of Santa Fe, No. SF 82-218(C) (November 22, 1989)

(SEAL)

STATE OF NEW MEXICO

FIRST JUDICIAL DISTRICT

November 22, 1989

FIRST JUDICIAL DISTRICT COURT
COUNTY OF SANTA FE
STATE OF NEW MEXICO

CAUSE NO. SF-82-218(C)

CONTINENTAL POTASH COMPANY, et al.,

Plaintiffs,

v.

FREEPORT-McMORAN, INC., et al.,

Defendants.

COURT'S FINDINGS OF FACT
AND
CONCLUSIONS OF LAW

(Nov. 22, 1989)

This case was tried to a jury. During the trial, the parties stipulated that the affirmative defenses would be given to the Court, as fact-finder. It was further stipulated that the Court would enter findings of fact and conclusions of law concerning the affirmative defenses if a need to do so existed. On July 7, 1989 the jury returned its verdict in open court. The jury having found that

certain breaches of duty took place, it is now incumbent on the Court to enter its findings of fact and conclusions of law relating to the affirmative defenses.

The following findings of fact and conclusions of law are entered by the Court. To the extent a finding of fact can or should be considered a conclusion of law, or a conclusion of law should be considered a finding of fact, it shall be so considered.

FINDINGS OF FACT

1. Walter M. Cross was a well-educated, sophisticated businessman and an inventor. In the 1940s, Mr. Cross prospected for potash in southeastern New Mexico and secured federal and state permits and leases relating to the potash-bearing lands he discovered.

2. In April 1949, Kansas City Testing Laboratories ("KCTL"), a Missouri corporation organized by Walter M. Cross, entered into an agreement with Freeport Sulphur Company ("Freeport") which granted Freeport the right to explore these potash-bearing lands and to earn an assignment of the permits and mining leases which had been issued by the United States government and the State of New Mexico. In this agreement, KCTL recited that the permits and leases had been assigned to it by Walter Cross, Ann Cross and J. G. Hawthorne and warranted that the permits and leases were its property (Exhibit 2). In an agreement dated April, 1948, Continental Potash Company ("Continental"), also formed by Walter Cross, had given Freeport permission to explore the identical lands and to acquire leases thereon. Continental

gave its express approval and consent to the 1949 agreement, in which Freeport was directed to pay a portion of KCTL's royalty to Continental.

3. The parties to the 1949 agreement contemplated that Freeport would become the direct lessee of the federal and state governments and operate a potash mine on the lands in question if Freeport elected to go forward with development.

4. The 1949 agreement also provided that in the event Freeport constructed and operated a mine it would be obligated to pay KCTL and Continental a royalty equal to 8% of the divisible profits from the production and marketing of potash from the properties subject thereto.

5. On March 1, 1951 KCTL and Freeport entered into a second agreement covering two additional mining permits. The terms of this agreement were substantially the same as those of the 1949 agreement, except that no provision was included that any portion of KCTL's royalty was to be paid to Continental. (Exhibit 3).

6. On March 1, 1951, Freeport also entered into an agreement with Mary Borders cross [sic], in which Mrs. Cross granted it an option to acquire another federal potash prospecting permit covering lands contiguous to the permits and leases mentioned above. In the 1951 Cross agreement, Freeport agreed to pay Mrs. Cross a royalty equal to 3% of the divisible profits from the production and marketing of potash from the lands or 1% of the selling price at the mine of potash produced and marketed, whichever was greater. Freeport subsequently exercised the option and was granted a lease by the United States. (Exhibit 4).

7. On December 28, 1953, Freeport entered into another agreement with Mary Borders Cross, in which Mrs. Cross granted it an option to acquire certain additional federal and state potash permits. As of December 1953, therefore, the contract between Freeport and the royalty holders consisted collectively of the 1949 agreement, the 1951 agreements and the 1953 agreement.

8. Freeport explored the potash lands covered by the agreements and ultimately decided to exercise the various options. The royalty holders consequently assigned their federal prospecting permits and leases to Freeport. The federal government granted Freeport leases on the balance of the lands shortly thereafter. (Exhibit 4). As of the early 1950's, therefore, Freeport was the direct lessee of the potash mining lands and the United States and State of New Mexico were its lessors. The Plaintiffs were royalty holders.

9. Defendants Freeport became the active, controlling party in the development of the mineral interests discovered and perfected by Plaintiffs (royalty holders), and the latter became the passive, dependent party in the development of the mineral interests. Freeport exercised full control and enjoyed superior knowledge of the operation over Plaintiffs.

10. There was no lessor-lessee relationship at any time between the Plaintiffs and the Defendants.

11. In 1955, with the consent of the federal and state governments, Freeport assigned all its potash leases to a corporation owned equally by Consolidation Coal Company and itself, the National Potash Company ("NPC"). (Exhibit 5, page 2).

12. As of the early 1950's, net profit royalty interests in certain of the potash mining lands in question were held by Mrs. Cross and by KCTL and Continental. KCTL was under the effective control of Walter M. Cross. The majority of shares in Continental had been sold to a group of investors headed by Mr. Milton McGreevy. Mr. McGreevy was a graduate of Harvard College and Harvard Business School, an officer in large national stock brokerage firm and sat on the boards of a number of corporations, including the Spencer Chemical Company, a buyer of potash. Like Mr. Cross, Mr. McGreevy was a sophisticated and knowledgeable businessman.

13. Sometime after the McGreevy group of investors purchased Continental, a dispute arose between Continental and KCTL concerning their respective royalty rights. On October 24, 1956, Continental, KCTL the former Mrs. Cross (now Mary Boarders Byrte) and NPC entered into an agreement which pooled all the royalty interests and also resolved the dispute between KCTL and Continental. From this point forward in these findings of fact and conclusions of law the pooled leases shall simply be referred to as the "Lea County Mine."

14. The 1956 agreement expressly superseded the royalty provisions (Exhibit 5, para. 9). It granted KCTL, Continental and Mrs. Byrte a cumulative net profit royalty. Whenever such a royalty was payable, 56-1/4% of such payment would be made to Continental, 28-3/4% to KCTL and 15% to Mrs. Byrte would be entitled to the greater of her share of the cumulative net profit royalty or an alternative gross receipts royalty.

15. In the 1956 agreement, the parties expressly ratified and confirmed the 1948, 1949, 1951, and 1953 agreements, to the extent that the terms and conditions of those earlier contracts did not conflict with the 1956 agreement. They continue to apply, except as modified by the 1956 agreement. (Exhibit 5, para. 9).

16. With regard to the marketing of potash, the agreements are silent except to provide that the calculation of the net profit royalty is computed on "the gross proceeds from potash sold to customers less all applicable allowances, discounts, bad debts, selling commissions . . . ", less all other allowable costs and expenses. (Exhibit 5, para. 2(b)).

17. Under the 1956 agreement NPC was to furnish the royalty holders with semi-annual statements of the results of its potash operations, prepared in accordance with good accounting practice and verified annually by an independent firm of certified public accountants. (Exhibit 5, para. 2(d) and (e)).

18. The net profit royalty agreement to in the 1956 agreement included what the parties called a "net loss carry-forward." Simply stated, this meant that if NPC went into production on the mining lands, it would only be required to pay a net profit royalty in a given fiscal year if any net loss which had accumulated prior to that year had been overcome.

19. Under the contracts which are the subject of this action, Freeport undertook to carry out the following implied covenants:

a. To do whatever in the circumstances would be reasonably expected of operators of ordinary prudence, having due regard for the interests of both Defendants and Plaintiffs;

b. To mine in a prudent and miner-like manner, maintaining the property and not damaging it through waste;

c. To market the product from the mine at the prevailing market price, which is the highest price obtainable by the exercise of reasonable effort;

d. To account to the Plaintiffs with fidelity;

e. To act all times with good faith to the royalty holders and with fair dealing, which, given Defendants' superior knowledge, included the duty to make timely, accurate and complete disclosure to Plaintiffs of material facts regarding the Lea County mineral reserve, mining operations, and accounts.

In addition, Freeport expressly agreed to avoid economic waste and to achieve ultimate maximum recovery within the meaning of those terms in the federal leases assigned by Plaintiffs to it and incorporated into the parties' agreement. Freeport breached each of these covenants and such breaches individually and collectively damages Plaintiffs.

20. Freeport's control extended to possession of all information concerning the enterprise, including mining and accounting information. Plaintiffs were totally dependent for information about the enterprise on Defendants, who were obligated to report periodically to the

Plaintiffs in statements of operations verified by a recognized national accounting firm under Generally Accepted Accounting Principles, referred to in the contracts as "good accounting practice."

21. NPC provided the required semi-annual statements and annual verifications to the royalty holders each year thereafter.

22. The contracts between the parties incorporated by reference the federal mineral leases to the potash deposit at issue here.

23. The 1948 contract (Exhibit 1) specified that the agreement would last so long as commercial production was obtained from the lands in question.

24. On the only occasions when NPC chose to abandon a particular lease, the lease was first offered to the royalty holders, in accordance with the relevant terms of the contract. In each instance, the royalty holders declined to receive assignments of those leases, and they therefore surrendereded [sic] to the federal government. See, e.g., Exhibits BT and BU.

25. With the exception of the leases mentioned in finding number 22, above, NPC did in fact keep all the leases in full force and effect at all relevant times, and in fact they have never been surrendered and are still in effect.

26. NPC operated the Lea County Mine from the time it opened in 1956 until 1968, when operations were temporarily suspended. The mine was not reopended [sic] on a full-scale basis again until 1976.

27. NPC told the royalty holders it would suspend operations in the Lea County Mine prior to the time it did so. (Exhibit AR). It did not misrepresent the reason for the suspension.

28. NPC's annual reports received by the royalty holders in the years 1969 through 1976, inclusive, showed that operations in the Lea County Mine were in fact suspended.

29. In the years 1969 through 1975, the royalty holders actually knew that NPC was not conducting any mining at all in the Lea County Mine.

30. At all relevant times, the royalty holders and their legal advisors were of the opinion that NPC had a legal duty to conduct mining operations in the Lea County Mine with reasonable diligence.

31. The royalty holders did not claim that NPC was failing to mine with reasonable diligence or that NPC had abandoned the Lea County operation during the six year period when operations were suspended or for more than five years after operations were resumed.

32. The royalty holders never claimed or demanded that NPC should surrender the federal or state potash leases or assign them to the Plaintiffs.

33. Paragraph 15 of the April, 1949 agreement (which was expressly incorporated in the 1956 agreement by paragraph 9 of that instrument) required KCTL to give Freeport advance written notification of any alleged default so that Freeport would have an opportunity to cure.

34. The royalty holders never notified Freeport or any of its successors of any alleged default or of a contention that failure to surrender the potash leases constituted a default.

35. Under the 1948 agreement, the leases in question should have been tendered back to the Plaintiffs on or about July 8, 1968, the date of shutdown, but were not.

36. Defendants failed to act as a reasonably prudent operator by keeping the leases and not surrendering them back to Plaintiffs when Defendants knew or should have known that there was no reasonable expectation of further commercial production beneficial to Plaintiffs from the lands given Freeport's lack of access to higher grade ore for blending with the Lea County ore. The duty to surrender was a continuing one on and after July 8, 1968.

37. Freeport's true reason for shutting down the Lea County mine was to concentrate its operations solely on a richer ore body in which no private royalty interest existed. It was Freeport's undisclosed intention to mine out this richer ore to exhaustion while mothballing the Lea County reserve but keeping it in its inventory for financing reasons. Freeport later changed itsmind [sic] by deciding to reopen the Lea County mine, but did so under extremely risky circumstances, the true extent of which were not disclosed to Plaintiffs.

38. Freeport deliberately concealed from Plaintiffs its true basis for the 1968 shutdown and retained the leases under false pretenses.

39. Plaintiffs reasonably relied upon Defendants' misrepresentations, omissions and concealments of material facts regarding the shutdown in not taking action to enforce their rights under the contractual agreements (Exhibit 1-5) until the filing of this action.

40. At all material times, Plaintiffs exercised due diligence in attempting to obtain information concerning the mining venture at issue here whether due diligence is measured by ordinary standards or a reduced standard applicable to relationships between a royalty holder and developer/operator of mining interests.

41. Plaintiffs reasonably relied on assurances from the highest sources at Defendants; corporate headquarters that the defendants were carrying out and fulfilling their obligations under the agreements.

42. Starting in 1959, Defendants blended Lea County ore (i.e., ore from the royalty holders' deposit) with higher grade ore and such blending produced net profits sufficient to overcome all cumulative losses and generate $78,190 royalty which was paid to Plaintiffs. This was the only consideration every paid to Plaintiffs by Defendants and represented 0.00068 (less than seven ten-thousandths) of the gross revenues of approximately $114,000,000 derived from the Lea County ore reserve from 1957 to 1982, when permanent shutdown occurred. Royalties based on gross revenues in the potash industry during material times ranged from 1% to 3.5% of gross revenues.

43. Defendants failed to act as a reasonably prudent operator of Lea County ore after July 8, 1968, by ceasing to blend Lea County ore with higher grade ore from

Defendants' richer Eddy County mine or with other high grade ore and instead mothballing the Lea County mine until the Eddy reserve with [sic] exhausted in 1976, without reasonable prospect of obtaining richer ore for blending thereafter.

44. In December, 1958 after the Lea County Mine was in operation, NPC entered into a potash sales agreement with Central Farmers Fertilizer Company (Hereafter referred to as "CFI") (Exhibit 8). By the terms of this agreement NPC agreed to sell and CFI agreement to buy the entire output of the Lea County Mine up to 500,000 tons per year, through 1974. The price CFI agreed to pay was "market price" less a discount. The discount was to be 4% for the first few years and then 5% once NPC retired certain indebtedness, plus an additional incentive discount which was contingent on the making of profits. (Exhibit 8, para 4, page 8). The parties established as a benchmark for determining market price the lowest price quoted and published on a given date by one Carlsbad producer and met by another Carlsbad producer (generally referred to during trial as the "Carlsbad list price"). Carlsbad list price did in fact represent the price at which Carlsbad producers were actually selling their potash at that time.

45. In their contract, NPC and CFI agreed that "market price", which was the key to their contract, would be determined by a method to be agreed upon by the parties or, failing that, by arbitration. (Exhibit 5, para. 3, page 6).

46. As it turned out, Carlsbad producers continued to publish prices, but the Carlsbad list price no longer

represented the actual market price of potash by the late 1960s.

47. Continental learned of the sales agreement between NPC and CFI in January 1959, about two weeks after it was signed. Milton McGreevy, who was president of Continental, wrote to NPC on January 14, 1959. In his letter McGreevy expressed Continental's concern that the selling agreement was not in the normal course of business and might therefore adversely affect NPC's profits and that this would, in turn, prejudice the royalty holders' prospects for receiving net profit royalty payments. (Exhibit 70).

48. Despite numerous inquiries by Plaintiffs about this agreement, Freeport made only partial and misleading disclosure about it to Plaintiffs and failed to correct statements which later became untrue as pricing structures in which the potash industry changed because of increasing competition from Canadian potash producers.

49. Defendants made statements regarding the marketing of the potash product which either were not true when made or became untrue thereafter and such statements were not correct by Defendants. Plaintiffs reasonably relied on Defendants' representation and assurances in not discovering that their rights under the agreements were being violated and had not [sic, i.e., no] reasonable basis for suspecting prior to four years before this lawsuit was filed that Defendants' statements were or had become untrue.

50. Potash is not publicly traded and information about potash prices is not available to persons outside the

potash industry. The only timely and accurate compilation of potash prices is that kept on a monthly basis by the Department of the Interior through the U.S. Geological Survey. By regulation, these compilations are considered proprietary confidential industry information by the USGS and at all relevant times were unavailable to Plaintiffs or their representatives. Plaintiffs thus had not means for discovering that statements made by Freeport concerning the reasonability of the price at which the product from the Lea County mine was being sold to CF were untrue and that in fact the discounts given to CF were substantially and unreasonably below market price.

51. Freeport's relationship with CF Industries, Inc. constitutes a naked conflict of interest.

52. Defendants failed to act as a reasonably prudent operator by failing to sell the product from the Lea County mine at the prevailing market price, which is the highest and best price obtainable by the exercise of reasonable effort. This breach damages Plaintiffs.

53. In the years 1980 and 1981, the price of potash on the export market ballooned so that the export realization was approximately 30% to 50% higher than Freeport's domestic realization. Freeport failed to market its product from the Lea County mine on the export market with reasonable effort. Had it done so, the then-accumulated loss carryforward would have been eliminated in those two years alone, net profits would have been generated in a significant amount, and substantial royalties would have been paid to Plaintiffs. The value of such lost royalties exceed $800,000.

54. At all relevant times Continental and KCTL had first-rate professional assistance, including attorneys and mining experts.

55. There is no language in the agreement between NPC and the royalty holders, or any of its constituent parts, which establishes a fiduciary or "confidential" relation between them.

56. In the latter part of the 1960s, new Canadian potash producers with lower production costs than Carlsbad potash started to sell substantial volumes of potash into the United States market. Prior to this time, most of the potash consumed in the United States was produced in the Carlsbad area. This introduction of significant additional supply disrupted the domestic market. Generally speaking, the "Carlsbad list price" of potash, which up to this time had been representative of actual market price, was no longer an accurate reflection of the true market price of the product in the United States. While Carlsbad list prices continued to be published, domestic producers discounted off of the published price in order to compete with the Canadian suppliers.

57. There is no evidence that any officer of NPC felt that NPC was required to send the royalty holders information about changes in the potash market or in the CF contract.

58. Starting in the spring of 1978 Defendants also failed to act as a prudent operator by highgrading the Lea County ore. Highgrading is a mining term of opprobrium and means the selective removal of higher grade mineral materials in order to artificially boost short term profits. The effect is to render the remaining mineral deposit

more expensive to retrieve and often, as in this case, impossible to retrieve commercially within a reasonably foreseeable time period. Defendants' highgrading program was reckless and in wanton disregard of Plaintiffs' interest and rights.

59. Defendants deliberately concealed their highgrading program from Plaintiffs and thus acted in bad faith, which damaged Plaintiffs by rendering approximately 5,000,000 tons of remaining product equivalent ore in the Lea County mine commercially unrecoverable. On the date of final shutdown, February 3, 1982, the remaining product tons in the ground had a then-market value of approximately $380,000,000 and a reasonable royalty value to Plaintiffs on that date in excess of $1,816,690.23.

60. Defendants committed economic waste, did not meet the standard of a reasonably prudent operator and damaged Plaintiffs in an amount equivalent to the reasonably [sic] royalty value accruing on date of final shutdown (February 3, 1983).

61. Defendants failed to act as a reasonably prudent operator by failing to account with fidelity and by charging Plaintiffs' account with improper charges under the parties' contract. This breach damages Plaintiffs in amount exceeding $300,000. These damages accrued after February 1976.

62. Under good accounting practice, Freeport should have, but did not, disclose in its semi-annual statements of operations to Plaintiffs the fact that CF Industries, Inc., was a "related party," an accounting terms [sic] which would have put Plaintiffs on notice that

sales to CF might not be at market prices. This undisclosed conflict of interest breached applicable standards of good accounting practice and damaged Plaintiffs.

63. Failure of Defendants to account properly to Plaintiffs regarding CF and to make proper accounting disclosures to them about CF damaged Plaintiffs.

64. Plaintiffs were entitled to rely upon the semi-annual statements of operations furnished under the contractual agreement to the Plaintiffs and there was no basis for suspicion that these semi-annual statements were not accurate until within four years prior to the filing of this action.

65. Freeport misrepresented or deliberately failed to disclose to Plaintiffs the following material facts:

A. The true marketing procedures and prices used in disposing of the Lea County product to CF;

B. The true reason for not surrendering the Lea County leases to Plaintiffs after July 8, 1968;

C. The true risks for Plaintiffs from reopening the Lea County Mine in 1976 without benefit of higher grade ore for blending;

D. The true level of New York overhead reasonably allowable by Freeport to its potash division and specifically to Plaintiffs' royalty account during the second run of production (1976-1982);

E. The highgrading program;

F. The true prospects for royalties during the second run of production while concealing knowledge

that the second run of production would most likely be no better than book break even and thus of no benefit whatsoever to Plaintiffs.

66. Each of these misrepresentations or omissions was committed knowingly and deliberately by Freeport or by wanton or reckless disregard for Plaintiffs' rights; their falsity was not known and not knowable by Plaintiffs through exercise of reasonable diligence; and Plaintiffs reasonably relied on them to their detriment.

67. As a commercial agreement, the contract between the parties included an implied covenant of good faith and fair dealing which the various concealments, misrepresentations and omissions of the Defendants, described herein, breached, causing damage to Plaintiffs.

68. Freeport had a company policy not to consult with or make full disclosure of material facts to its royalty holders including Plaintiffs. At all material times Defendants acted in conformity with this policy to Plaintiffs' detriment. Defendants concealed the existence of this policy from Plaintiffs and Plaintiffs had no reason to suspect its existence. The policy breached Defendants' implied covenant of good faith and fair dealing including disclosure of all material facts. This breach was willful and deliberate. The policy was malicious and in wanton disregard of Plaintiff's rights.

69. Defendants acted in bad faith, maliciously, willfully and recklessly and with reckless disregard for Plaintiffs' rights in selling the Lea County product to CF at

substantial discounts off market prices under circumstances constituting a conflict of interest, thereby defeating Plaintiffs' chances to realize royalties; failing to continue blending Lea County ore with higher grade ore; failing to surrender the leases after determining that commercial production could not longer be achieved; reopening the Lea County mine in 1976 without disclosing the true risks of this venture to Plaintiffs; concealing the growing crisis for their potash operation after 1976 from Plaintiffs; inflating New York overhead charges in the second run of production, high-grading the Lea County mine, failing to properly exploit the export market in 1980 and 1981; and failing to act as a reasonably prudent operator in negotiations for sale of the potash business to another producer.

70. Breach of Freeport's duty to surrender the leases first occurred July 8, 1968 and caused at least $1,816,690.23 damage (not including interest) to Plaintiffs representing the value of their royalty interest at that time.

71. The misrepresentations, concealments and omissions of the Defendants recounted in Findings 64 and 68, above, constituted fraud and caused damage to Plaintiffs in the amount of at least $1,816,690.23. Damages for the fraud involving the 1968 shutdown were in this same amount and first accrued July 8, 1968. Said fraud was continuing and took place through and including the date of filing of this suit.

72. The damages for failure to surrender the leases (Finding No. 69) are coincident with the sum of damages

for waste, accounting breaches and market breaches accruing after February 2, 1976.

73. The damages for failure to surrender the leases and other breaches of contract (Finding No. 71) are coincident with the damages for fraud.

74. Defendants were under a contractual obligation to develop the Lea County mine and consequently Defendants' investment in the Lea mine did not constitute prejudice.

75. Defendants were not prejudiced by any delay of the Plaintiffs in filing this action.

76. Defendants had unclean hands and are thus not entitled to assert any equitable defense.

77. Plaintiffs made inquiry from time to time concerning Freeport's marketing and mining operations. These inquiries were voiced directly to the highest sources at Freeport. Each time, Defendants gave reassurances that no breaches of duty by Freeport were occurring. Given the circumstances on each occasion, Plaintiffs reasonably relied to their detriment on these reassurances and had no reasonable grounds for further investigation. The reassurances constituted fraudulent concealments of material fact and lulled Plaintiffs into repose. Plaintiffs had no cause to suspect they were being defrauded until within the four-year period immediately proceeding the filing of this suit.

78. The actions and omissions of the Defendants in deliberately failing to make disclosures of material fact to Plaintiffs on a regular, continuing and complete basis shock the conscience of this Court and serve as grounds

for equitably tolling the statutes of limitation which might otherwise bar portions of this action.

79. In any event, independent of all claims arising before 1976, the jury's compensatory award of $1,816,690.23 is substantiated by fraud and breaches of contract committed by Defendants with reckless and wanton disregard for Plaintiffs' rights, in bad faith, maliciously, wantonly or deliberately within six years preceding the filing of this action and four years in the case of fraud.

CONCLUSIONS OF LAW

1. The Court has jurisdiction of the persons and subject matter of this lawsuit.

2. By stipulation of the parties, the Court was granted the power to act as fact finder of all questions pertaining to affirmative defenses and prejudgment interest.

3. With regard to issues of fact found by the jury as to the legal claims of the parties which overlap issues of fact (such as fraud) concerning the matters now before it, the Court concludes that there is substantial evidence to support each of the jury's express and implicit findings.

4. The parties had a contractual relationship under which certain implied covenants were imposed by law as well as in fact. These include:

A. To do whatever in the circumstances would be reasonably expected of operators of ordinary prudence, having due regard for the interests of both Defendants and Plaintiffs;

B. To mine in a prudent and miner-like manner, maintaining the property and not damaging it through waste;

C. To market the product from the mine at the prevailing market price, which is the highest price obtainable by the exercise of reasonable effort;

D. To account to the Plaintiffs with fidelity;

E. To act at all times with good faith and fair dealing as regards to the Plaintiffs, which included the duty to make timely, accurate and complete disclosure to Plaintiffs of material facts regarding the Lea County mineral reserve, mining operations, and accounts.

5. Plaintiffs exercised reasonable diligence to uncover the breaches of contract and frauds on which their claims were based.

6. Plaintiffs [sic] efforts to inform themselves of the truth about their interests fulfilled the due diligence requirement for equitable tolling of the statute of limitations as measured by the standard applicable to ordinary commercial relationships at arm's length.

7. Plaintiffs had no reasonable means for learning the true facts regard their mining interests except from Defendants, who as a result, had a legal duty, which they breached, to keep Plaintiffs fully informed.

8. Defendants fraudulently concealed Plaintiffs' causes of action.

9. Defendants committed a continuing fraud upon Plaintiffs by silence, misrepresentation, omission and concealment of material facts. Said continuing fraud

caused damages to Plaintiffs which coincide with the damages caused by their breaches of contract as found by the jury and also constituted fraudulent concealment for purposes of the statute of limitations.

10. As to all of Plaintiffs' claims, to the extent that any of them accrued more than the relevant period of time set in applicable statutes of limitation before the filing of this lawsuit, this Court concludes that any bar to the filing of such claims was equitably tolled by reason of Defendants' deliberate fraudulent concealment and none of the affirmative defenses should be granted.

11. As to the defense of laches, this Court concludes that such defense is not well taken in that Defendants were not prejudiced by any delay of the Plaintiffs in filing this action and in any case the commission of fraud in the nature of fraudulent concealment by Defendants constitutes unclean hands and overcomes the defense as a matter of law.

12. The Court further concludes under the doctrine of accrual that the jury's verdict as to compensatory damages renders the affirmative defenses irrelevant since all of the award is supported by substantial evidence of breaches of duty committed by Defendants occurring within any applicable limitations period.

13. The verdict of the jury as to damages is supported by substantial evidence and is not subject to reduction or elimination on the basis of any of the affirmative defenses and those defenses are as a matter of law not well founded.

14. The Plaintiffs should be given judgment in the full amount of the jury's verdict. The Court reserves for further ruling the Plaintiffs' application for prejudgment interest and interest from date of verdict to date of filing of judgment.

/s/ Petra Jimenez Maes
PETRA JIMENEZ MAES,
District Judge
Division One

I hereby certify that on this 22 day of November, 1989, a true and correct copy of the foregoing was mailed to counsel of record:

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Secretary, Division I

APPENDIX N

NMSA 1978, SCRA 12-404(A)

12-404. Rehearings.

A. Motion; when filed. A motion for rehearing may be filed within fifteen (15) days after filing of the appellate court's disposition, or any subsequent modification of its disposition, unless the time is shortened or enlarged by order. The three (3) day mailing period set forth in Rule 12-308 does not apply to the time limits set by this rule. The motion shall state briefly and with particularity, but without argument, the points of law or fact which in the opinion of the movant the court has overlooked or misapprehended. If the motion is based upon a point of law or fact not raised, briefed or argued by any party but relied upon by the court in its disposition of the matter, the motion shall specifically so state, and shall be accompanied by a brief in support thereof. In all other cases the movant may, but is not required to, file a brief in support of the motion at the time it is filed. No response to a motion for rehearing shall be filed unless requested by the court. If a motion for rehearing is granted, the appellate court clerk shall give notice thereof and any party who has not filed a brief on rehearing may, within ten (10) days after notice, file a brief addressed to the issues on rehearing. There shall be no other briefs or argument unless the appellate court shall otherwise direct.

* * *

APPENDIX O

30 CFR 231.12, 231.13, and 231.14 (in force when operations began)

§ 231.12 *Lessee shall observe good practice.* The lessee shall observe good practice in prospecting and mining, sinking wells, shafts, and winzes, driving drifts and tunnels, stoping, blasting, transporting ore materials, hoisting, the use of explosives, timbering, pumping, and other operations for the development and preservation of any operation, mine, or mine equipment on the lease.

§ 231.13 *Operations shall be conducted in a manner to yield ultimate maximum recovery; information recorded and copy furnished district mining supervisor.* Mining operations shall be conducted in a manner to yield the ultimate maximum recovery of the mineral deposits. All shafts, main exits, and passageways, as well as overlying beds or mineral deposits that at a future date may be of economic importance, shall be protected by adequate pillars in the deposit being worked. Information obtained regarding the mineral deposit being worked and other mineral deposits on the leased lands shall be fully recorded and a copy of the record furnished to the district mining supervisor.

§ 231.14 *Sufficient pillars shall be left.* Sufficient pillars shall be left in first mining to insure the ultimate maximum recovery when the time arrives for the removal of pillars. Boundary pillars shall in no case be less than 50 feet thick unless otherwise specified in writing by the mining supervisor. Boundary and other main pillars shall be mined only with the written consent or by order of the mining supervisor or his authorized subordinates.

APPENDIX P

Excerpt from Rothwell memorandum of February 1, 1973, Trial Exhibit 221, *Continental Potash, Inc., et al. v. Freeport-McMoran, Inc., et al.*, District Court of New Mexico, County of Santa Fe, No. SF 82-218(C)

February 1, 1973 Ex. 221

Mr. Grossman

Mr. Rothwell

Either in 1968 or earlier, National Potash Company dropped three of the eight leases it held on the Lea County deposit. It continues to hold five leases.

In 1968, prices were in a disastrous decline which reached its low point in the fall of 1969 at which time prices were approximately half their present level. At that time there was no expectation of substantial improvement since the decline had been caused by an influx of high quality, low cost potash from Canadian mines which were being brought on stream and expanded at a rapid rate.

National could not, however, abandon the Lea County leases at that time without substantially reducing its "reserves" and therefore the theoretical "life" of its Carlsbad operation. Most of the funds needed for the development of that operation had been borrowed from Metropolitan Life Insurance Company, and under the terms of that borrowing, National would have been required to prepay the debt if its reserves dropped to a point at which it no longer had sufficient for five years of operation beyond the 1974 scheduled maturity of the debt. Abandonment of the Lea County deposits would

have reduced National's "reserves" and shortened its "life" to considerably less than five years after that maturity date.

Rothwell
10-19-87

AFR:e

Continental Potash Co.
V
Freeport-McMoran Inc.
Santa Fe County District Court SF
82-218(C) 12593
PLAINTIFFS' EXHIBIT 221

APPENDIX Q

Excerpts from Appellees' Answer Brief showing cites to evidence in support of attacked findings, New Mexico Supreme Court, No. 19,054 (May 24, 1993)

IN THE SUPREME COURT
OF THE STATE OF NEW MEXICO

CONTINENTAL POTASH, CO., et al., Plaintiffs-Appellees, and Cross-Appellants, -vs- FREEPORT-McMORAN, INC. et al., Defendants-Appellants, and Cross-Appellees.	No. 19,054

APPEAL FROM THE DISTRICT COURT OF
SANTA FE COUNTY, JUDGE PETRA JIMENEZ MAES

APPELLEES' ANSWER BRIEF
(Filed Feb. 12, 1991)

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Appendix A

EVIDENCE IN SUPPORT OF ATTACKED FINDINGS

SCRA 1986, § 12-213(A)(3) provides that any contention a finding is not supported by substantial evidence is waived unless the party contending includes in his Summary of Proceedings the substance of the evidence bearing on the proposition. *Salinas v. John Deere Co., Inc.*, 103 N.M. 336, 707 P.2d 27 (Ct.App. 1985). The Brief in Chief at page 19 attacks no less than 38 of the Court's findings without including the substance of the evidence. The following evidentiary references without being all-inclusive show there was substantial proof to support each one:

FINDINGS ATTACKED AS "WITHOUT LEGAL OR EVIDENTIARY SUPPORT"

39 **[Detrimental reliance]** Exhibits 93, 103, 108, 139, 169, 221, 226; TR 116-19, 139-43, 148-57, 474, 476-77, 493-501

41 **[Reassurances]** TR 117-18, 396, 476-77, 479-82; and *see* Finding 39 above

48 **[Misrepresentations and omissions; marketing]** Exhibits 11 (NPC minutes of 3-13-62), 70, 72, 73, 76, 139; TR 139-42, 487, 1006; and *see* Finding 39 above

49 **[Lulling; marketing]** Exhibits 11, 139; TR 396-410, 487, 621, 701, 853-59, 1010; Nelson Deposition, 48

50 **[Marketing; superior knowledge]** TR 143, 253-58, 310-12, 453, 474, 482, 485, 487, 607, 763, 1010, 1122-28, 1132-39, 1141, 2349-51; Nelson Deposition, 250-51

65A **[Fraud; marketing]** Exhibits 8, 11 (Minutes of 3-13-62), 72, 76, 139, 362 [p. 2, top], 367, 370 [¶ 9], 378 [pp. 12-15], 425, 454; TR 139-42, 374-78, 396-98, 402-10, 419-37, 659, 667-70, 701, 881-85, 1006, 1010, 1767, 1847, 1865-66, 1876, 1887, 2006-16, 2031-35; Nelson Deposition, 111, 133-34

65B **[Fraud; surrender]** Exhibits 169, 186, 221; TR 148-57, 385

65C **[Fraud; risks of reopening]** Exhibit 174, 331, 495, 487 [p. 2]; TR 1006, 1033-36, 1050-60, 1063, 1195, 1316

65D **[Fraud; accounting]** Exhibits 7, 7A, 154, 304, 308, 313, 319, 344, 345, 350, 357, 463G, 485; TR 171-79, 240-47, 301, 331-37, 387-92, 886-92, 917-18, 1165, 1661, 1917-25, 1946, 1989, 2023-30, 2049-59, 2338-39, 2474-75; Nelson Deposition, 101-4

65E **[Fraud; highgrading]** Exhibits 307, 308, 312, 314, 317, 326, 331, 338, 340, 354, 355, 445 [p. 11], 484; TR 167-70, 746-57, 764-68, 796, 798, 821-26, 1064-90, 1251, 1258-59, 1324, 1691, 2095, 2135, 2281, 2324-25, 2328; Nelson Deposition, 148-50; and *see* Finding 59 below

65F **[Fraud; prospects for royalties]** Exhibits 319, 322, 329, 331, 334, 345, 357, 370

66 **[Fraudulent concealment; punitive damages]** Exhibit 186, 221, 226; TR 143, 148-70, 312, 378, 382, 670, 870-73, 879-85, 1303, 1691, 2030, 2035, 2274-77; and *see* Findings 65, 68, 77.

68 **[Policy not to consult or inform]** TR 148-70, 382, 405-6, 670, 1006-10, 1547-48, 1691, 2030-35, 2057

69 **[Fraudulent willful breaches]**

(Discounts, conflict of interest) Exhibits 11, 322 [pp. 15-16], 367, 370, 425, 454; TR 621, 651, 667-68, 703-7, 879-85, 1151, 1706-7, 1767, 1822, 1860-66, 1875, 1877-78, 1887, 2006-16; Nelson Deposition, 44, 51, 133-34

(Failure to blend) Exhibits 1, 3 (paragraph 8), 164, 174, 174A; TR 766, 1041-47, 1050-55, 1195, 1227-28, 1240, 1310-21, 1598, 1745, 2503-10

(Failure to disclose true risks of reopening) TR 1040-43, 1317; and *see* Finding 65C above

(Failure to surrender) Exhibits 1 [¶ 7(d)], 186, 212, 221, 322 [pp. 14-16], 331 [esp. p. 4], 370; TR 102, 108, 385; *see* Findings 15, 23 below

(Concealing growing crisis) Exhibits 322, 329, 331, 335, 345, 350, 357, 370

(Inflating New York overhead) Exhibits 7, 7A, 319, 463G, 485; TR 171-77, 240-49, 331-37, 387-92, 886-91,

917, 1661, 1917-25, 2023-29, 2049-57, 2338-39; Nelson Deposition, 101-4

(Highgrading) Exhibits 338, 340, 354; TR 167-70, 634, 747-57, 764, 796-98, 821-26, 1064-90, 1258-59, 1324, 1691, 2095, 2135, 2156, 2281, 2324-25, 2328; Nelson Deposition, 148-50; and *see* 65E

(Export failure) Exhibits 15, 377, 378 [p. 1], 384 [p. 2], 387, 412 (column 4, line 4); TR 438-453, 612, 667-68, 692-93; Nelson Deposition, 132-34

(Sale of business) Exhibits 420, 427, 428, 441; TR 359, 455-70

70 **[surrender damages]** Exhibits 1, 164, 174, 179, 186, 212, 221, 445 [p. 7], 463E, 463F; TR 385, 904-15, 1040-43, 1060, 1177-86, 1195, 1322-24

71 **[Fraud damages coincident with contract damages]** *See* Findings 64-68, 70

75 **[No prejudice from delay]** Exhibits 1-5, 319; Nelson Deposition, 377-78

76 **[Unclean hands]** *See* Findings 65, 66, 69

77 **[Reasonable reliance; lulling]** Exhibits 70, 72, 73, 76, 102, 103, 137, 139, 158, 163, 169, 226, 266, 304, 313, 344, 345, 350; TR 116-19, 143, 474-87

78 **[Shocked conscience]** *See* Findings 48, 49, 50, 59, 62, 65, 66, 68, 69 and 77

FINDINGS "ATTACKED IN BRIEF"

9 **[Superior knowledge and control]** Exhibits 1-5; TR 127-78, 441, 474-501, 701, 706-8, 1006-10, 1458, 1657-58; Nelson Deposition, 226

19 **[Implied covenants]** Conclusion of law: see Nelson Deposition, 212-18; *Brewster v. Lanyon Zinc*, 140 F.

801; *Darr v. Eldridge*, 66 N.M. 260; *Freeport Sulphur v. American Sulphur Roy. Co.*, 6 S.W.2d 1039; Merrill, "Implied Covenants Between Others than Lessors and Lessees," 27 Wash. U.L.Q. 155

20 **[Control of information; duty to disclose]** Exhibit 5 [pp. 7-8]; TR 382, 383, 873, 879-85, 1006-10, 1657-58; Nelson Deposition, 226

22 **[Federal requirements incorporated]** Exhibit 3 (1951 Agreement), paragraph 8: "subject to the requirements of the federal leases . . . "

35 **[1948 Surrender provision]** Findings 15, 23; Exhibits 1, 176, 212; TR 102, 108, 385, 1682-83

36 **[Continuing duty to surrender]** Exhibits 174, 186, 221; and *see* Findings 69, 70 above

37 **[Shutdown]** Exhibits 174, 174A, 186, 221, 331

38 **[Fraudulent concealment of true reason for shutdown; surrender breach]** Exhibits 169, 186, 221, 226; TR 151-57

40 **[Due diligence]** TR 117-18, 130-34, 143, 171-78, 258, 312, 474-77; and *see* Findings 48, 49, 50, 65, 66, 68 above

43 **[Blending; imprudent mining]** TR 766-68, 1041-50, 1195, 1316, 1745, 2401-2; Nelson Deposition, 61-62, 423-24

51 **[Conflict of interest]** Exhibit 154 [pp. 8-10]; TR 703-7, 882-85, 1767, 1822, 1860-66, 1877-78, 1887, 2031-35; Nelson Deposition, 44, 51, 302-4, 308

52 **[Marketing breach]** Exhibits 7, 12, 13, 14, 181, 367, 370, 378 [pp. 12-15], 454, 463, 463A; TR 374-77, 419-53, 667-68, 898, 1122-39, 1151, 1287-92, 1862-66, 1887, 2006-16; Nelson Deposition, 133-34, 293; and *see* Finding 65A above

53 **[Export fiasco]** TR 438-53, 612; Exhibits 15, 377, 384 [p. 3], 391 [p. 1], 400 [p. 1], 412

58 **[Highgrading]** Exhibits 308, 312, 314, 331, 338, 340, 354, 445 [p. 11] 484; TR 746-57, 764-68, 798, 821-26, 1064-90, 1251, 1258-59, 1324, 2095, 2135, 2156, 2273, 2281, 2324-25, 2328; Nelson Deposition, 148-50

59 **[Waste; value of residual ore]**

(Concealed highgrading) TR 167-70, 903-16, 1006, 1691; and *see* Finding 70 above

(Commercial tonnage rendered unrecoverable) Exhibits 16, 379, 383 [These exhibits show that commercially recoverable ore reserves stood at approximately 27,000,000 tons as of January 1980 but that as of date of closing, February 1982, the "ore reserve" (defined as "mineral concentrations which can be mined on a profitable basis" had dropped to nil]; TR 454, 626-27, 673, 1042, 1258-60, 1324; Nelson Deposition, 176

(value) TR 1177

60 **[Waste; damages]** Exhibits 463E and F; and *see* Finding 59 above

61 **[Accounting breaches]** Exhibits 154, 319, 345, 350, 463G, 485; TR 171-78, 240-49, 301, 331-337, 387-92, 814, 886-91, 917-18, 1165, 1661, 1917-25, 1946, 2023-30, 2048-57, 2338-39; and *see* Finding 65D above

62 **[Failure to disclose related party]** Exhibit 154; TR 880-85, 2031-35 (Eads reluctantly admits it)

63 **[Accounting breach damages]** Exhibit 463G; TR 885-92, 1984

64 **[No basis for suspicion]** Mixed fact/law Finding; *see* Findings 39, 41, 48, 49, 50, 65A, and 65F above

67 **[Breach of good faith]** Conclusion of law (implied covenant of good faith)

74 **[No prejudice from developing mine]** Conclusion of law

79 **[Post-1975 damages]**

(Highgrading) Exhibits 338, 340, 354, 469 [no. 20]; TR 747-57, 764, 768-69, 821-26, 1064-90, 1165-70, 1174-89, 1258-59, 3124, 1691

(Creative accounting) Exhibits 7A, 319; TR 240-49, 331-37, 387-92, 814, 885-92, 917, 1923, 1984, 1989, 2023-28, 2049-57; and *see* Findings 65D, 69 [Inflating New York overhead], 71 above

(Mismarketing) Exhibits 463, 463A; TR 419-53, 612, 667-68, 2006-16; and *see* Findings 52, 53 above

(Sale of business) Exhibits 420, 427, 428, 441, 445 [p. 11], 469 [nos. 20, 21]; TR 359, 455-70

(Writedown of 5 million product tons proven reserves) Exhibits 17 [10-K's], 446, 448; TR 454, 673, 1177, 1179; Nelson Deposition, 176-77

In a case with much evidence, Defendant has skillfully summarized evidence which might have supported a judgment in its favor. The question, however, is not whether the evidence would have supported a different result, but whether evidence exists to support the result that occurred. *Clovis Nat'l Bank v. Harmon*, 102 N.M. 166, 692 P.2d 1315 (1984); *Tapia v. Panhandle Steel Erecting Co.*, 78 N.M. 86, 428 P.2d 625 (1967); *Sundt v. Tobin Quarries, Inc.*, 50 N.M. 254, 175 P.2d 684, 169 ALR 586 (1946).

APPENDIX R

Excerpts from Defendants' Second Amended Set of Proposed Jury Instructions, *Continental Potash, Inc., et al. v. Freeport-McMoran, Inc., et al.*, District Court of New Mexico, County of Santa Fe, No. SF 82-218(C) (July 6, 1989)

FIRST JUDICIAL DISTRICT COURT
COUNTY OF SANTA FE
STATE OF NEW MEXICO
No. SF 82-218(c)
CONTINENTAL POTASH, INC., et al.,

Plaintiffs,

vs.

FREEPORT-McMORAN INC., et al.,

Defendants.

DEFENDANTS' SECOND AMENDED SET OF PROPOSED JURY INSTRUCTIONS

The defendants Freeport McMoran, Freeport Minerals and National Potash Company, pursuant to ¶ 10 of the Pretrial Order governing this case submit their Amended First Set of Proposed Jury Instructions.

Respectfully submitted,

MONTGOMERY & ANDREWS, P.A.

By /s/ Deborah S. Dungan
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(505) 982-3873

Attorneys for Freeport Defendants

DEFENDANTS' PROPOSED JURY

INSTRUCTION NO. 14

Duty to Operate.

National had an implied duty to operate the mine as a prudent operator would operate the mine.

GIVEN: _____

REFUSED: _____

GIVEN AS MODIFIED: ✓ PM

See e.g. *Clayton v. Atlantic Refining Co.*, 150 F. Supp. 9 (D.N.M. 1957)

DEFENDANTS' PROPOSED JURY

INSTRUCTION NO. 15

Prudent operator defined.

When I say in these instructions that National was required to act as a prudent operator, I mean that National was required to act as any reasonable mining company would act under similar circumstances, with due regard for its own interests as well as the interests of its lessors or royalty holders. National had no obligation to carry on operations that would not be profitable to National, even if some benefit to Continental might have resulted.

GIVEN: _____

REFUSED: ✓ PM

GIVEN AS MODIFIED: _____

See Clayton v. Atlantic Refining Co., 150 F. Supp. 9 (D. N.M. 1957)

DEFENDANTS' PROPOSED JURY

INSTRUCTION NO. 16

Duty to market.

National had an implied duty to exercise good faith and diligence to sell the potash produced from Continental's properties at the "prevailing market rate."

GIVEN: _____

REFUSED: ✓ PM

GIVEN AS MODIFIED: _____

See e.g., Greenshields v. Warren Petroleum Corp., 248 F.2d 61 (10th Cir.), *cert. denied*, 355 U.S. 907 (1957); *Craig v. Champlin*, 300 F.Supp. 119, 125 (1969); 5 Williams & Meyers Oil & Gas Law § 856.3 p. 408.

DEFENDANTS' PROPOSED JURY

INSTRUCTION NO. 17

Efforts to market evaluated under prudent operator standard.

National's efforts to market the potash produced under its agreement with Continental should be evaluated under the prudent operator standard.

GIVEN: _____

REFUSED: ✓ PM

GIVEN AS MODIFIED: _____

5 Williams & Meyers, *Oil and Gas Law* § 856.3, p. 407; *See, e.g., Greenshields v. Warren Petroleum Corp.*, 248 F.2d 61 (10th Cir.), *cert. denied*, 355 U.S. 907 (1957)

DEFENDANTS' PROPOSED JURY

INSTRUCTION NO. 24

Uncertainties of exploration and development require a lessee to regard its own interests as well as lessor's interests.

The large expense incident to the work of mineral exploration and development, and the fact that National would bear the loss if the operations were not successful, required that National proceed with due regard for its own interests, as well as those of royalty holders like Continental.

GIVEN: _____

REFUSED: ✓ PM

GIVEN AS MODIFIED: _____

See 5 Williams & Meyers, *Oil and Gas Law* § 806.3, p. 36; *Brewster v. Lanyon Zinc Co.*, 140 F. 801, 814 (8th Cir. 1905)

Supreme Court, U.S.
FILED
JAN 21 1994
OFFICE OF THE CLERK

No. 93-994

IN THE
Supreme Court of the United States
OCTOBER TERM, 1993

CONTINENTAL POTASH INC. and
CROSS LABORATORIES, INC.,
Petitioners,

v.

FREEPORT-MCMORAN, INC., FREEPORT MINERALS CO.,
and NATIONAL POTASH CO.,
Respondents.

On Petition for a Writ of Certiorari to the Supreme Court of the State of New Mexico

---

BRIEF OF RESPONDENTS IN OPPOSITION

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QUESTIONS PRESENTED

1. Whether the Supremacy Clause is properly invoked by private parties in a case where it was never alleged that the federal government's regulatory or proprietary functions were affected.

2. Whether the United States Supreme Court has jurisdiction to entertain a petition for certiorari in a case where the petitioners asserted the existence of a federal question for the first time in a motion for rehearing in the Supreme Court of New Mexico.

3. Whether the United States Supreme Court has jurisdiction to entertain a petition for certiorari in a case where the petition was not filed for more than four months after a motion for rehearing in the State Supreme Court was denied.

PARTIES TO THE PROCEEDINGS

The caption of the case contains the names of all parties.

Freeport-McMoRan, Inc. is the corporate successor of Freeport Minerals Co. Freeport Minerals Co. was the corporate parent of National Potash Co. while National Potash Co. was vital. All the shares of National Potash Co. were assigned to a third party in the early 1980s, with Freeport-McMoRan, Inc. retaining all liabilities and obligations accruing prior to the date of the assignment.

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On Petition for a Writ of Certiorari to the Supreme Court of the State of New Mexico

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BRIEF OF RESPONDENTS IN OPPOSITION

SUMMARY OF ARGUMENT

The parties to this litigation are private business concerns. They entered into a contract in which the petitioners assigned federal prospecting permits and mineral leases to Freeport.[1] In the contract, the petitioners expressly agreed that, as between them, Freeport would have the unilateral right to determine which ore it would mine and which ore it would leave unmined. Freeport was the direct mineral lessee of the United States. The

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[1] For purposes of convenience, we shall refer to the respondents, collectively, as "Freeport."

federal leases imposed specific duties on Freeport, duties Freeport owed to the United States. The federal leases remained unamended and were fully enforceable by the government at all relevant times.

The issues in this lawsuit involved only the private contract the petitioners had with Freeport. The questions addressed by the Supreme Court of New Mexico were purely questions of New Mexico law, i.e., the law of contract and contractual construction. The United States was not a party to this litigation and its interests were never involved.

The petition for certiorari represents an attempt to make a private contractual dispute appear to be one involving the federal government and federal interests. There is no question of law at issue that justifies the granting of a writ of certiorari.

REASONS WHY THE WRIT SHOULD BE DENIED

I. THERE IS NO FEDERAL QUESTION IN THIS CASE

In *Equitable Life Assurance Soc'y v. Brown*, 187 U.S. 308 (1902), the Court said ". . . not every mere allegation of a Federal question will suffice to give jurisdiction. 'There must be a real substantial question on which the case may be made to turn,' that is, a real, and not a merely formal, Federal question is essential to the jurisdiction of the Court." 187 U.S. at 311 (citing *City of New Orleans v. New Orleans Water-Works Co.*, 142 U.S. 79 (1891)).

This is a case in which there has never been a federal question. Accordingly, this Court lacks jurisdiction to entertain the petition for certiorari. *Martin v. Hunter's Lessee*, 14 U.S. 304 (1816); *Murdock v. City of Memphis*, 87 U.S. 590 (1874).

Counterstatement of the Case

In the 1940s, two closely-held corporations, Continental Potash Company and Cross Laboratories, Inc., held a number of federal prospecting permits pertaining to land in southeastern New Mexico. The land contained substantial deposits of potash, a material used in the manufacture of fertilizer. Neither Continental nor Cross had the wherewithal to construct or operate a potash mine. Accordingly, they entered into a contract with Freeport. The contract provided that the prospecting permits would be assigned to Freeport, who would then obtain federal mineral leases from the government and decide whether to construct and operate a mine. If Freeport decided to proceed, and actually did mine potash, it agreed to pay the petitioners an eight percent royalty on whatever cumulative net profits might result from its efforts. (Pet. A5-6).

The parties agreed that decisions relating to the operation of the mine would be left to Freeport alone:

> ". . . the nature and extent of all work done by Freeport on the mining lands and the time and manner of doing the same shall rest in the sole judgment and discretion of Freeport"

The contract also stated that:

> "subject to the requirements of the leases, the nature and extent of all exploration, development and mining operations and the time and manner of performing the same shall be as Freeport in its sole judgment and discretion shall determine and Freeport shall have the right at all times to determine the quantity of ore to be mined and what ore is to be left unmined . . ."

The petitioners had no ownership interest in the mineral bearing lands. They were simply net profits royalty holders whose rights were set out in a written contract with Freeport. (Pet. A5-7). Nothing in the contract

affected the independent interests, rights or powers of the United States.

Freeport also owed responsibilities to the government, as provided in the mineral leases and the relevant federal statutes and regulations. Thus, Freeport had two different legal relationships, with different entities. One relationship, with the petitioners, was governed by a contract. The other, with the United States, was governed by a cluster of federal mineral leases and various federal statutes and regulations. The United States was not dependent on the private net profits royalty holders to enforce its rights. Indeed, the government had no relationship with the net profits royalty holders of any kind. (Pet. A6).

That the government's rights affecting Freeport's operation of the leases were more encompassing than those of the private royalty holders is undeniable. The federal leases specifically gave the United States the power to halt mining operations if it believed Freeport was committing economic waste, such as by "highgrading." The United States also had the power to cancel the mineral leases if it felt Freeport breached its obligations. 30 U.S.C. § 188; *see Dawn Mining Co. v. Watt*, 543 F. Supp. 841 (D.C. D.C. 1982), aff'd, 704 F.2d 1293 (D.C. Cir. 1983).

The petitioners' lawsuit sounded in contract. The government was not a party. The petitioners did not contend (as they do now) that they represented the interests of the United States in "enforcing federal anti-waste provisos incorporated into the contract of assignment." (Pet. 15). They contended only that the operative provisions of the government's leases were part of their private contract. (Pet. J1-2; K1). The trial judge eventually held that the terms of the federal mineral leases were incorporated by reference in the private contract. (Pet. M-7). At trial, however, the question for the jury, as posited by the court, was whether Freeport had breached

some alleged implied contractual covenants. (Pet. A2; L).

Accordingly, the question of contract interpretation before the Supreme Court of New Mexico was whether this private contract contained implied covenants. Employing principles of contractual construction which are by no means unique to New Mexico jurisprudence, the court concluded that the contract was too specific in its language to admit of the alleged implied covenants. (Pet. A30-39).

The New Mexico court pointed out that the United States, as Freeport's lessor, could have brought an action for waste if it believed there were grounds for doing so. (Pet. A38-39). But the court also made it absolutely clear that this case involved only the rights and duties of the parties before it, rights and duties which were governed by state law.

In *City of New Orleans v. New Orleans Water-Works Co.*, this Court held that "the bare averment of a federal question is not in all cases sufficient. It must not be wholly without foundation. There must be at least color of ground for such averment, otherwise a federal question might be set up in almost any case, and the jurisdiction of this court invoked simply for the purpose of delay." 142 U.S. at 87.

The petitioners cannot make a purely private contract become an instrument of federal importance.

II. THE NEW MEXICO COURT'S JUDGMENT RESTS SOLELY ON NONFEDERAL GROUND

The Supreme Court has no jurisdiction to review a state court judgment resting on an adequate non-federal ground. *Herb v. Pitcairn*, 324 U.S. 117 (1945). If the state court decides only non-federal questions, or decides both federal and non-federal questions, the Supreme Court has no jurisdiction to review if the non-federal

ground is adequate to support the judgment. *New York Times Co. v. Jascalevich*, 439 U.S. 1317 (1978).

Every issue touched upon in the Supreme Court of New Mexico's opinion flows from the private contract. The conclusions reached by the court are summarized at the end of its opinion:

> "In sum, the trial court erred in holding that the breach of contract claims and the fraud claim are not barred by the applicable statutes of limitations. The trial court abused its discretion in tolling the statutes of limitations. The record does not support the trial court's finding of fraudulent concealment nor the application of equitable estoppel to preclude the defendants from asserting the statute of limitations defenses. The trial court also erred as a matter of law in finding and enforcing implied covenants against the defendants."

(Pet. A41-42).

To say that the non-federal ground is adequate to support the judgment is to understate the case. The non-federal ground is the *only* ground of decision. There is no federal issue in the case and, therefore, no federal ground for the New Mexico decision to rest on. The resolution of this dispute did not require or involve analysis of the Mineral Leasing Act of 1920, the terms and conditions of the federal mining leases or the rights and interests of the United States. None of these subjects is addressed in the New Mexico court's decision.

Petitioners' Authorities Distinguished

The petitioners cite a number of cases dealing with inapposite situations. They begin with *Ventura County v. Gulf Oil Corp.*, 601 F.2d 1080 (9th Cir. 1979). In that case, a California county was not permitted to enforce its zoning ordinances controlling oil and gas exploration on federal lands. No one in the case at bar tried to prevent the federal government from exercising its right to regulate Freeport's mining operations.

The petitioners next argue that unless the New Mexico judgment is overturned, there will be a hodge-podge of decisions affecting mining operations on federal leaseholds, with no uniform rule to follow. The case they cite, *Lowey v. Watt*, 684 F.2d 957 (D.C. Cir. 1982) dealt with the BLM's authority to administer the Oil and Gas Leasing Program under the Mineral Leasing Act of 1920. The court in *Lowey* distinguished the case before it from *Wallis v. Pan Am. Petroleum Corp.*, 384 U.S. 63 (1966). The point made by the *Lowey* court is directly applicable here:

> "*Wallis* was a diversity case, a contract dispute between two private parties of no concern to the federal government except for the fact that their dispute involved a federal lease. These cases, in contrast, arise on petitions for review of administrative decisions; the duties of federal officials in administering the noncompetitive leasing program are directly in issue."

684 F.2d at 966.

There is no danger of lack of uniformity. The New Mexico court makes it clear that it is only construing the terms of a contract between a mining company and some private net profits royalty holders. Nothing in the court's decision is binding on the United States or in any way affects the United States in the administration of its mineral leasing program. The court even reminds the reader that the rights of the United States are separate, distinct and fully enforceable.

In *Wallis v. Pan Am. Petroleum Corp.*, the question before this Court was whether a contract dispute between private parties dealing with a federal lease was governed by federal or state law. The Court said:

> We find nothing in the Mineral Leasing Act of 1920 expressing policies inconsistent with state law in the area that concerns us here. In providing for develop-

> ment of public domain lands containing minerals, the Act comprehensively regulates various aspects of the process. For example, it governs issuance of leases among competing applicants, e.g., § 17(b), (c), 30 U.S.C. § 226(b), (c); it controls in some measure the actual use of the leased tract, to promote goals such as conservation and safety, e.g., § 30, 30 U.S.C. § 187; and it deals with rent and royalty payments to be made to the Government, e.g., § 17(d), 30 U.S.C. § 226(d). Few provisions lend themselves at all to the creation of a federal law of the rights *inter se* of private parties dealing in the leases.

384 U.S. at 69.

The Court went on to say this:

> Finally, it is said that because the leases are issued by the United States and concern federal lands, there is a federal interest in having private disputes over them justly resolved. Apart from the highly abstract nature of this interest, there has been no showing that state law is not adequate to achieve it.

384 U.S. at 70-71. Also *see Shoshone Mining Co. v. Rutter*, 177 U.S. 505 (1900) (a suit by adverse claimants for a patent under the federal mining law is not a suit arising under the laws of the United States in such a way as to confer jurisdiction on a federal court).

The petitioners mischaracterize the New Mexico decision when they say it "sanctions mining practices forbidden by federal law." (Pet. 19). The decision does not sanction anything. It interprets a contract. In that contract, private royalty holders, who did not have an ownership interest in the mineral bearing lands or the minerals themselves, agreed that they would have no participation at all insofar as mining decisions were concerned. By contrast, the United States, as lessor, retained significant prerogatives regarding the conduct of operations by its lessee.

The court did not "fail to recognize a private cause of action for highgrading." (Pet. 19). Whether a given litigant can seek damages for highgrading depends on the nature of its relationship with the mining company and the terms of its contract. The federal leases gave the United States such a cause of action. The petitioners' contract did not.[2]

United States v. Ruzicka, 329 U.S. 287 (1946) is cited for the argument that the ruling below "significantly impedes administration of the mineral leasing program." (Pet. 23) The question before this Court in *Ruzicka* was whether a handler of milk could resist a claim against him by the Secretary of Agriculture, made according to procedures defined in the Agricultural Marketing Agreement Act of 1937, without previously having sought to challenge the claim in a proceeding before the Secretary. *Ruzicka* has nothing to do with any issue in this case, real or imagined.

The petitioners cite *Rothensies v. Electric Storage Battery Co.*, 329 U.S. 296 (1946) as supporting the argument that the ruling of the New Mexico court "stands as a serious hinderance to effective administration of the law." *Rothensies* dealt with a technical accounting question in the tax law. It is hard to imagine a case having less to do with the issues resolved by the Supreme Court of New Mexico.

Petitioners claim that *Morton v. Ruiz*, 415 U.S. 199 (1974) points up how the decision of the New Mexico court "is at odds with well established construction of the Mineral Leasing Act by the Secretary of the Interior." In *Morton v. Ruiz*, this Court held that general assistance

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[2] The court did not hold that "highgrading is beneficial." It merely pointed out, in *dicta*, that the holder of a net profits royalty is benefitted whenever the miner pursues a program aimed at generating a profit. It was the court's way of distinguishing the positions held by the holder of a net profits royalty and the owner/lessor of the mineral estate. (Petition for Certiorari, A 38-39)

benefits are available to Indians if they live near their reservation and maintain close economic and social ties with it. The case has nothing to do with the Mineral Leasing Act.

United States v. Coleman, 390 U.S. 599 (1968) is said to support the contention that the New Mexico court's decision has a "specific impact on the utilization of public lands." In *Coleman*, the litigants were the United States and a party who claimed to have discovered a valuable mineral deposit. The question before the Court was whether the United States was required to convey the land to the claimant. *Coleman* is one of countless examples of how the government looks after its own interests and is not dependent on a private party for that function. *Coleman* and cases like it highlight the lack of a federal question in a case such as this one.

In *United States v. Mitchell*, 463 U.S. 206 (1983), this Court held that the United States is accountable in money damages for alleged breaches of trust in connection with its management of forest resources on allotted lands of the Quinault Indian Reservation. *United States v. Mitchell* has nothing to do with the question of whether federal revenues are affected by the New Mexico court's decision in this contract dispute between non-governmental parties. Since the United States can enforce the terms and conditions of its mineral leases, statutes and administrative regulations, the decision of the New Mexico court has no potential effect on government revenues.[3]

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[3] The government's royalty was not based on Freeport's profitability. It was based solely on the gross production of ore and was paid whether the company made a profit or not. *See* 30 U.S.C. § 282; *United States v. Southwest Potash Corp.*, 352 F.2d 113 (10th Cir. 1965).

III. THE PETITION FOR CERTIORARI IS PROCEDURALLY DEFECTIVE

A. The Petitioners Raised the Purported Federal Question Too Late to Confer Jurisdiction on This Court

If there is a true federal question, it must be raised and decided at the trial level to be preserved for Supreme Court review. If both of these do not appear on the record, appellate jurisdiction fails. *Cardinale v. Louisiana*, 394 U.S. 437 (1969); *Owings v. Norwood's Lessee*, 5 Cranch 344 (1809). If the alleged federal question was only tangentially involved below, the Supreme Court lacks jurisdiction to entertain a petition for certiorari. *Garrity v. State of New Jersey*, 385 U.S. 493 (1967); also see 28 U.S.C. § 1257 and S. Ct. R. 14(h).

At trial, the petitioners contended that their contract with Freeport gave them rights and powers normally associated with ownership of the mineral estate, i.e. rights and powers identical to those enjoyed by the United States. The petitioners did not contend that they took over the government's regulatory function.

On appeal, the question was what rights and powers the contract gave the petitioners as against Freeport. At no time did the petitioners contend, as they do now, that the interests of the United States were involved. The argument that the government's interests were somehow invaded was introduced to this litigation for the first time in the amended motion for rehearing *en banc*, filed May 24, 1993 in the Supreme Court of New Mexico, after the court's decision had been filed (Pet. F-2). This is too late. *Cox Broadcasting Corp. v. Cohn*, 420 U.S. 469 (1975); *Radio Station WOW, Inc. v. Johnson*, 326 U.S. 120 (1945).[4]

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[4] It is also too late under New Mexico law. *See Ellis v. Citizens' Nat'l Bank of Portales*, 25 N.M. 319, 183 P. 34 (1918); *Mosely v. Magnolia Petroleum Co.*, 45 N.M. 230, 114 P.2d 740 (1941). Thus,

It must appear affirmatively from the record not only that the federal question was presented for decision to the highest court of the state having jurisdiction but that its decision of the federal question was necessary to the determination of the cause. *Honeyman v. Hanan,* 300 U.S. 14 (1937). The opinion filed by the Supreme Court of New Mexico makes it clear that a resolution of the "federal question" advanced now by the petitioners was not necessary to the determination of the case. Obviously, an issue cannot have been necessary for resolution of a case if it was not mentioned by the court and not even raised until after the case was decided.

The argument that the New Mexico court's holding caught the petitioners by surprise is incorrect. Freeport's theory of the case, as argued from the earliest stages, was that the petitioners had no contractual right to demand that any particular mode of mining be followed. The petitioners certainly knew what the effect on their case would be if the state court were to agree with Freeport. If the petitioners truly believed that the government's ability to enforce its leases would somehow be impaired if they lost their private net profits royalty claim, they should have raised the issue in the trial court.. *Herndon v. Georgia,* 295 U.S. 441 (1935).

B. The Petition For Certiorari Was Filed Too Late

Supreme Court Rule 13.4 provides:

> "[I]f a petition for rehearing is timely filed in the lower court by any party in the case, the time for filing the petition for a writ of certiorari for all parties (whether or not they requested rehearing or joined in the petition for hearing) runs from the date of the denial of the petition for rehearing or the entry of a subsequent judgment. A suggestion made to a United States court of appeals for a rehearing

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there would be an independent state law ground for rejecting the petitioners' argument even if it had merit.

in banc pursuant to Rule 35(b) Federal Rules of Appellant Procedure, is not a petition for rehearing within the meaning of the Rule."

The relevant chronology in this case is as follows:

Decision of the Court	April 22, 1993
Motion for Rehearing *En Banc*	May 5, 1993
Amended Motion for Rehearing *En Banc* (alleged federal question introduced to the case)	May 24, 1993
Motion for Rehearing Denied	August 10, 1993
Second Motion for Rehearing *En Banc*	August 24, 1993
Second Motion for Rehearing *En Banc* Denied	September 24, 1993
Petition for Certiorari Filed In the United States Supreme Court	December 21, 1993

Supreme Court Rule 13.4 contemplates that a party shall have one bite at the rehearing apple before the time to prepare and file a petition for certiorari begins to run. In this case, the petitioners took their bite on May 5, 1993 and learned the outcome on August 10, 1993. They did not file their petition for certiorari until more than four months later. The time to file the petition expired on November 8, 1993. The petition for certiorari, filed December 21, 1993, came too late to invoke this Court's jurisdiction.

CONCLUSION

The Supreme Court of New Mexico dealt only with issues of state law. It construed a contract between private parties and determined their respective rights and duties pursuant to that contract. The independent rights of the United States were not litigated or affected in any way, at any time. The alleged federal question was not articulated until after the Supreme Court of New Mexico

filed its decision and the petition for certiorari itself was filed unseasonally. It is respectfully submitted that the petitioners have wholly failed to sustain their burden to establish that there are special and important reasons why the writ should be granted.

The petition for certiorari should be denied.

Respectfully submitted,

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REPLY TO BRIEF IN OPPOSITION

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REPLY TO BRIEF IN OPPOSITION

I. THERE IS A SUBSTANTIAL PREEMPTION QUESTION AFFECTING IMPORTANT MINERAL INTERESTS OF THE UNITED STATES.

1. By recognizing that the federal leases and regulations were incorporated into the parties' agreement (Pet. A8) and then deciding in the face of those regulations (and contractual commitments to abide by federal law) that highgrading did not breach the contract, the court below necessarily reached the federal issue. The holding that highgrading accords with federal law (Pet. A38) will not stand and cannot be reconciled with the Supremacy Clause. *Wallis v. Pan American Petroleum Co.*, 384 U.S. 63 (1966); *Boesche v. Udall*, 373 U.S. 472 (1963); *Lowey v. Watt*, 684 F.2d 957 (D.C. Cir. 1982); *Dawn Mining Co. v. Watt*, 543 F.Supp. 841 (D.C.D.C. 1982), *affirmed* 704 F.2d 1293 (D.C. Cir. 1983). *Wallis* and *Lowey* compel state courts as well as federal courts to apply federal law whenever interpretation of private contract rights under the Act significantly impacts the federal program.

2. The Opinion below holds that highgrading comported with Respondents' covenant of good faith and fair dealing under State law. (Pet. A38) Yet federal law incorporated into the contract required Respondents to employ "reasonable diligence, care and skill," "prevent undue waste," and work towards "ultimate maximum recovery." 30 U.S.C. § 187; Pet. I, J2. In *Cook v. El Paso Nat. Gas Co.*, 560 F.2d 978 (10th Cir. 1977), the court harmonized a contract assigning a lease issued under the Mineral Leasing Act with federal laws against wasting potash so as to

preserve an assignor's cause of action for failure of the assignee to protect her property while giving effect to federal conservation interests. Here, the New Mexico Supreme Court made no effort to reconcile federal and state law. Federal law already holds that highgrading is wasteful and breaches standards under the Mineral Leasing Act. *Dawn Mining, supra.* Here, however, the New Mexico court ignored this rule and held highgrading inactionable by a royalty holder, even though that activity ruined the Government's as well as the Petitioners' reversion and was forbidden by federal law.

By insisting that the State court made its ruling below only on State law grounds, the Brief in Opposition begs the question at the heart of this Petition: Whether the New Mexico Supreme Court was obligated to apply federal law to the contract issues surrounding highgrading.

II. THE COURT HAS JURISDICTION.

1. The federal anti-waste regulations (Pet. O) and lease terms incorporated by reference in the contract of assignment were in evidence at trial (Pet. G, H, I, J, O). The regulations were the subject of unopposed instructions to the jury, which was also instructed that the federal leases and regulations were incorporated into the parties' contract. (Pet. J2) Based on these instructions, the jury found that highgrading occurred and that it constituted a breach of contract damaging Petitioners. Respondents do not challenge the finding that highgrading occurred. The jury's verdict (Pet. L) was therefore based on federal law. Nothing more was needed to preserve the preemption issue.

2. The jury based its computation of damages on highgrading. (Pet. A13, n. 6) And the Opinion below notes that highgrading occurred within the limitations period. (Pet. A30) Thus, the Opinion's holding on highgrading was indispensable to the New Mexico court's resolution. The false statement that highgrading was "in furtherance of the royalty holders' interests" (Pet. A38; *but see*, Pet. L2, M15, M16, M21, Q4, Q7, and Q8) was the centerpiece of that holding because it made it possible to declare that highgrading did not breach the contract, even though that contract incorporated the federal leases and regulations (and applicable case law, *e.g., Dawn Mining*) as acknowledged in the Opinion. (Pet. A8) In consequence, there was no adequate state law ground for the ruling below and this Court has jurisdiction. The idea that highgrading benefits a royalty holder is untenable and cannot serve as an independent state ground sufficient to bar Supreme Court review. *Ward v. Love County*, 253 U.S. 17, 22 (1920); *Postal Tel. Cable Co. v. Newport*, 247 U.S. 464 (1918); and *see*, Stern, Gressman & Shapiro, *Supreme Court Practice* (6th ed.) 179.

3. The chronology on page 13 of the Response omits important circumstances. The unpublished memorandum decision of April 22 was vacated August 10, 1993, when the New Mexico Supreme Court significantly modified and published a new ruling as an Opinion. (Pet. A2, C2, C8) Under New Mexico procedure, NMSA 1978, SCRA 12-404(A) (Pet. N1), the motion for rehearing filed August 23, 1993 (Pet. D1) was timely. When the court below considered and denied that motion September 23, 1993,

the ninety-day period for filing in this Court began pursuant to Supreme Court Rule 13.1. This Petition was filed within the ninety-day period.

III. THERE IS AN IMPORTANT DUE PROCESS QUESTION AS WELL.

The Response fails to address the Due Process violations in Question 3 of the Petition. Although this Court does not often accept cases for review which rest on a State court's subterfuge, obfuscation or mischaracterization of the record, it should take, and in the past has taken, cases such as this one where the due process violations by a State high court not only injure private persons but also adversely affect important interests of the United States. *Kern-Limirick Inc. v. Scurlock*, 347 U.S. 110, 121 (1954); *Union Pac. R. Co. v. Public Service Com'n*, 248 U.S. 67 (1918); Stern, Gressman & Shapiro, *supra*, at 187.

FOR THESE REASONS, the Petitioners pray that the writ of certiorari issue.

Respectfully submitted,

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